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THE FINANCIAL SYSTEM OF INDIA

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WITH A FOREWORD BY

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TO

PROF. P. K. TELANG, M.A., LL.B.

OF BENARES

FOR ALL THAT THE AUTHOR OWES TO

HIS PRECEPT AND EXAMPLE

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PREFACE

The object of the book is to describe and examine the working of the Indian Financial System. It is a hazardous task, and would, probably, not have been undertaken but for the fact that till the end of 1923 there was no book in the field to which an ordinary reader could have an access to understand the constitution and the principles of the system of financial administration in India. In December, 1923, Mr. P. K. Wattal, M.A., of the Indian Audit and Account Service, brought out his book, "The Financial Administration of British India." By that time the present work had already been planned and almost half finished, and it was considered desirable to complete it on the assumption that the difference in treatment would justify its publication. The book is now presented to the public, and it is hoped that it will be found useful by all who take an intelligent interest in matters with which it deals.

It is not necessary to say much about the scope of the book. It deals with things as they are and as they might be. I have taken the liberty to comment on and criticize the working of the present system freely and make constructive suggestions, as far as possible. The merits of the system have always been kept in mind, and emphasized in view of the importance and necessity of conserving the gains of the existing order. The recognition of its merits has made it possible to point out its shortcomings without an uneasy feeling of being prejudiced against it. In India the study of the Financial System has so far been neglected in spite of the great interest that the financial questions have aroused since the beginning of the National Movement. The absence till the Reforms of popular control of

finances, which alone could have given significance to the desire and effort to understand it, is one of the reasons which account for this general indifference. The reason does not exist now. The introduction of partial popular control of finances and growing determination of the nation to make it more real and extensive are very good reasons for studying thoroughly the principles and practical working of the present system. It is assumed that the public is already alive to the need of acquiring this knowledge, and the book will, therefore, satisfy a real demand. The national problem in India is many-sided and complex, and it is possible that this book may, in some measure, be helpful in understanding it more fully.

The book has been written for the general public, but it is expected that it will specially appeal to the scientific students of the subject. Finance is, to use Mr. Mellon's phrase, the people's business; but it is also an intricate business and the people need more light, which must come from the Universities—our centres of learning. The Indian Universities have till recently neglected the subject of finance, and though problems of public revenue and expenditure have of late received greater attention, those of financial administration have not yet come to their own. The Hindu University has recently recognised the importance of the subject and instituted courses of studies for B.A.(Honours) and M.A. classes, but the other Universities have not considered it worth while to give it a place in their curricula. It is pre-eminently desirable that this indifference should pass away, and the study of the subject be cultivated in a scientific spirit. The book may perhaps be of some use in stimulating a scientific interest in the study of the subject and lead others to investigate its different aspects more thoroughly.

For the foreign student the study of the Indian Financial System has an interest of its own. India is not yet a democracy, but her Financial System has certain features which make it worthy of consideration. In its working may be traced the combination of different and in some

respects divergent tendencies, and the fact that it is in a state of flux gives to it an interest which it otherwise would not possess. The book does not aim at giving a comparative view of the subject, but it will be possible for the students of financial administration in other countries to study the general principles in the working of the Indian System. In the arguments of the book special pains have been taken to distinguish the wood from the trees, and details of the System have been explained with reference to general principles of wide applicability. The book will, it is hoped, on that account commend itself to the attention of the academic students all over the world.

Every care has been taken to ensure the accuracy of the information given in the book, but the fact that I have not had the opportunity of acquiring a personal knowledge and experience of the working of the system suggests the need of putting in a word of caution. It is possible that there may be in the book some errors of fact in spite of an earnest effort on my part to eliminate them altogether. It is hoped that they are very few and not important enough to vitiate the soundness of the arguments of the book.

The Indian System is in the making. The changes are being introduced every now and then to make it work smoothly under the new conditions. The book was completed in July, 1924, and during the interval some changes have been made. The most important ones are :—separation of Railway from General finance, introduction of the Debt Redemption Scheme, institution of Provincial Loan Fund, and separation of Audit and Account on the East Indian Railway as an experimental measure. An appendix on separation of Railway from General finance has been added in which the reasons which have led to the introduction of the reform, and financial procedure which is going to be followed under it, are briefly described. On other measures short footnotes have been added. But it is possible there may be some omissions, which, however, cannot be helped for obvious reasons.

It is not necessary to add that in this book India means British India. The Native States have been omitted altogether. They are in different stages of political development, a number of them have not got any financial systems worth speaking of, and those that may be said to have some sort of system of financial administration do not generally court publicity in matters with which we are concerned. It would be, moreover, impossible to deal with the financial system of the latter in the same book in which the financial system of British India is described. They are so different.

I have for reasons, for which no one can be blamed, not been able to have the benefit of having my manuscript read or my views examined by those whose friendly criticism would have been of very great value. This is a serious disadvantage. I am sure the book would have been improved in many ways if it had been possible to make changes in it in the light of the suggestions of well-informed friends. That fact, however, makes it clear that the responsibility for the shortcoming of the book and the views expressed in it is entirely mine. But that does not obviate the necessity of expressing my indebtedness to those who have helped me in other ways. My thanks are due to Mr. A. C. McWatters, the Finance Secretary of the Government of India, who kindly gave me very useful information regarding the official publications bearing on the subject. The Finance Secretaries of the Government of the United Provinces, Bombay, Bihar and Orissa, are also entitled to thanks for their having sent me the Budget Manuals of their respective provinces. Mr. E. A. H. Blunt, the Finance Secretary of the United Provinces, very kindly sent me his "Note on the Financial Administration under the Reform," which I have found very useful. The Director, Central Bureau of Information, has always answered my queries promptly and courteously, for which I am greatly indebted to him. Prof. J. C. Coyajee, of the Presidency College, Calcutta, now a member of the Currency Commission, has helped me in various ways, and I

owe him my sincere thanks for all that he has done for me. My friend, Prof. Brij Narain of the Sanatan Dharam College, Lahore, has lent me some of his rare blue-books which I could not have done without. Babu Shiva Prasad Gupta, the Hon'ble Raja Moti Chand, Pandit Iqbal Narain Gurtu, Dr. N. J. Shah and Munshi Madho Prasad—all of Benares—have kindly allowed me to use their blue-books and thereby laid me under their obligation. There are other friends to whom I owe more than I can tell. I cannot thank them adequately. All that they have done and the spirit with which they have done it make it impossible for me to express my feelings. I cannot do better than maintain strict silence about their many acts of friendship, and can best show how greatly I appreciate them by cherishing their memory with all the sincerity that I can command.

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FOREWORD

An organized State is a great factory in which machines of many different sorts are at work upon various processes. A factory has its engine-house, in which is placed the prime mover, the steam or electric engine that supplies power to all other machines. So in the State also there is an engine-house. It is the Finance Department or the Treasury; and in that is placed the financial engine which keeps all the machines of the Government at work, turning revenue into public services, just as a steam-engine turns coal into power.

This central machine, the financial prime mover, is that part of the machinery of the government which it is most essential for the public to understand. The smooth working of financial machinery depends upon three things in particular. The machine itself must be well planned. It must be in the hands of servants of the State who have the highest possible standard and tradition of integrity and assiduity. Last, and not least, its working must be steadily illuminated by the light of an instructed public opinion. It is vain to expect any financial organization, however perfectly devised, in the hands of any servants of the State, however faithful and diligent, to work at its best unless there is at least a strong element in public opinion that understands its working, that takes interest in it, and that is both able and ready to administer the stimulus of instructed and reasonable criticism. Informed

public opinion is the best safeguard of financial regularity and efficiency.

If any one of us wants to understand an engine in a factory, the first thing which he does is to ask somebody who understands it already to explain it to him; and if he is not so fortunate as to know any such person, he reads a text-book in which the structure and working of the machine are described. The man who wrote the text-book has done him a service. My friend, Professor Gyan Chand, has, I think, done a true service to the cause of good government by writing this book to explain the structure and working of the machinery of the financial system of India. He has provided the basis necessary for the formation of a well-informed public opinion in a matter vital to democratic progress.

It is, therefore, a privilege for me to be allowed to write this Foreword to a book which appears to me to achieve with distinction a task of the highest utility. Professor Gyan Chand writes with wide knowledge and with great lucidity. He knows how to take his machine to pieces, to distinguish its essential from its non-essential parts, and to fit the pieces together again, so as to show the function which is performed by each in relation to all the others. The ideal for such a book, no doubt, is that it should be as much explanatory, and as little controversial, as possible. That ideal, no doubt also, is unrealizable when the theme is a financial system so experimental and provisional as that of India. But to one reader at least it appears that Professor Gyan Chand's criticisms (as to the merits of which he is not qualified to judge) are made with moderation, and admirably illustrate his most useful appeal that financial policy should be separated, so far

as it is possible to separate it, from the arena of the party strife.

I guess that I may owe the privilege of introducing this book to the circumstance that the task which our author has here performed has been undertaken by me in respect of the financial system of Great Britain. Having laboured in the field, I know how arduous it is to till, and I can express with the conviction of experience my warm appreciation of the harvest that has been reaped. It is well cultivated, well matured, and well garnered.

E. Hilton Young.

Benares,
December 18*th*, 1925.

THE FINANCIAL SYSTEM OF INDIA

CHAPTER I

INTRODUCTION

A SOUND state of finance is of paramount importance for the political health of a nation. The slightest dislocation in that part of the body politic produces sometimes acute but more often chronic disorders in the national economy, and has, unfortunately, cumulative effect in undermining the very basis of national existence. The soundness of public finance depends both upon the right policy and good organization; but a great deal depends upon the latter, as the most unexceptionable financial policy is likely to be ineffectual, if not actually harmful, unless the mechanism for its execution is both adequate and effective. The constitutional history of England is, to a large extent, the history of the struggle of the people to gain control of the treasury and secure the supremacy of the common will. The victory has been won in England, and the popular control of the public purse is as complete or conclusive as it can be. The system is not perfect and has its aberrations; but it is a good system, and the political stability of England is, in no small measure, due to it. The other advanced countries in the world have, in their political development, evolved their own systems. These have necessarily been affected by the peculiar political and economic conditions of those countries. But the systems as they are, form an integral part of their national life,

and give the characteristic tone to the working of their political systems.

India is in a state of transition. Her national life is still lacking in certain vital elements of progress and efficiency. The political struggle has just begun. The first step in the direction of establishing a national and democratic State has already been taken. With the progress of events the situation becomes more and more complex, and often baffling. The future is a matter for speculation. That she has to pass through a vicissitude of political fortunes may be accepted as the cardinal fact of her present situation. The end is neither predictable nor in sight. She will, in the course of her political evolution, work out her own financial system, which, on account of the exigencies of the struggle and peculiarities of her national life, will have its own distinctive features. But it is very unlikely that the future developments will involve a complete breach with the present system. It will be changed under the stress of new forces, and changed in some essential respects. But it is difficult to conceive the possibility of the present system not having very important effect on making the financial organization what it will become in course of time. It is, on that account, a matter of profound importance for the politician, who is working with an eye to the future, to understand the present financial system, and acquire a thorough grasp of its basic features. The time will come, if it has not come already, when India will claim and get the right to determine her own political system in her own way. An intimate knowledge of the financial system will then be a great asset for our constitution makers, for India, like every other country, must have a sound financial system, organically connected with the rest of her national life. The present system has, from this point of view, to be thoroughly understood with its merits and shortcomings, and incorporated in the new system for expressing the national will, and making it flexible enough to secure the continuity of national growth.

The present financial system has a living interest for us from another standpoint as well. It is well known and generally accepted that increased popular control over the political system of the country must carry with it the control of the public purse. In England, since 1866, almost the whole public expenditure has been made subject to the Parliamentary approval, and the recognition of this right was the result of the victory of the democratic forces, which first manifested themselves in a feeble way in 1215. In India the same right has to be established, and the extent to which it is done will be the measure of the political power of the people of India. This does not mean merely that the Indian Legislatures, Central and Provincial, should have complete authority over the financial legislation, but also that they should exercise a comprehensive control over all branches of financial administration. They should have the means of examining the working of the whole system, and discovering and removing any flaws that such an examination may reveal. Finance, from the nature of things, is a very intricate business. The experts who know its mysteries can, if they so choose, defeat the intentions of the uninitiated legislators, unless they know that they cannot do it with impunity. In India the experts are, for some time to come, likely to be men who will be out of sympathy with the political aspirations of the people. The control of the Legislatures will, in order to be real, have to be made more far-reaching and constant than it is in some other countries. The consideration is a very strong reason for getting to know the intricacies of our financial machinery. The political progress of the country will require that the financial policy should be formulated and carried out according to our will as expressed through our accredited representatives. We should know how the system works and make it work for our ends. The vested interests will not surrender this power. The prospect of our having it will depend upon the fighting strength that we can put in the political field. But its intelligent and effective use, when it comes to our

hands, will depend upon our knowledge of the esoteric side of our finances.

Democracy in India will, by common consent, arise out of an alert and politically awake electorate. It is admitted that the urgent need of the hour is political education of the voters. A knowledge of civic rights and responsibilities must, of course, take the first place in any scheme of political education. "No taxation without representation," is, however, a time-honoured and fundamental principle of popular governments, and implies that it is the business of the tax-payer to acquaint himself with the system of raising and spending public money for the use of this political right. The diffusion of information regarding the financial practices and methods of the State is of very great importance for imparting a sound political education to the citizens of a free State. When the ballot-box means anything at all to the Indian voter, it will also mean that he should know how the financial affairs of the country are managed or mismanaged, as the case may be, and be able to cast his vote with a view to secure efficiency and purity in financial matters. It is, perhaps, too much to expect that he should know the system in its details. That has not been for an average voter in any part of the world. A working knowledge of its salient features should, however, not be beyond his ken, and must be an essential part of his training for the discharge of his political duties.

For the student of the financial problems a knowledge of the financial machinery is, of course, an imperative necessity. The politically minded Indians have had, since the beginning of the National Movement, a great deal to say against the financial sins of omission and commission of the bureaucracy. The methods of raising revenues and the objects on which they have been spent have come in for a great deal of criticism. The criticism has, however, not been very well informed in most cases. A Gokhale might, occasionally, take his adversaries aback by the amount of uncanny knowledge which he displayed

about the mysteries of the financial craft. But ordinarily the bureaucrat has held a vantage ground against his opponents on account of his intimate knowledge of the financial organization, which his position, given a moderate capacity for taking pains, easily enabled him to acquire. The Indian critics, for want of that knowledge, have not been able to play their rôle very effectively in the past. They will, in future, tilt in vain against the evils which all this time have aroused their reforming zeal, unless they are fully equipped with weapons which only the knowledge of technique can place at their disposal. It is worth while for those who aspire to expound or expose the financial policy of the Indian Government to understand the arrangement by which the policy is put into effect. The task is not as pleasant as the general condemnation of the policy of the Government for ever-increasing military expenditure or the crushing burden of taxation, but it is not less worth doing on that account. When it is realized that the discharge of public duty calls for as much knowledge as enthusiasm, and in the financial matters particularly, the former is the better part of the latter, the dull work of comprehending the hidden side of the national finances will acquire a new interest and a stimulating quality. With the wider opportunities for affecting the Government policy, this aspect of the matter should have an imaginative appeal which otherwise it would not possess.

The academic interest in the study of our financial system does not require any emphasis. For the student of the science of Public Finance, it is, of course, of utmost importance that he should be quite at home in dealing with the system on which the financial business of the nation is conducted. The problems of equity or incidence of taxation or the propriety or otherwise of a particular line of public expenditure are likely to have something elusive about them if the *modus operandi* of getting or spending the public money is not fully understood. It is as necessary for him to know the working of the system, and say how far it is sound, as to sit in judgment on the

political or economic effects of the financial policy of the state.

The considerations urged in the foregoing paragraphs will, it is hoped, afford sufficient justification for undertaking the study of the Indian financial system. It is not proposed to give a detailed account of its working in this small book. The object of this book is to give the broad outlines of the system and explain its basic principles. The starting point of our study must be the analysis of some fundamental features of the system, the understanding of which will be helpful in following the contents of the later chapters.

Finance is the incident of administration, and there must, therefore, be a very close connection between the administrative and the financial systems. The principle of the Indian administration, which the Reforms have neither affected in theory nor in practice, is that the Secretary of State, as the constitutional adviser of the Crown in all matters relating to India, has full powers of superintendence, direction, and control of the whole system of Indian administration, and the Government of India is required to pay due obedience to all such orders that it may receive from him. As an extension of the same principle the Secretary of State is supreme in all financial matters, and "the expenditure of the revenue of India, both in India and elsewhere, is subject to the control of the Secretary of State in Council." The relaxation of control, which the recent constitutional changes have effected, is not sufficiently great to affect the position substantially. The India Office is still the controlling centre of the Indian financial organization and the Secretary of State its chief regulator. The whole system has been so developed that nothing of importance can happen without his cognizance, and the various changes which have been introduced recently have not impaired the reality of his control. This essential fact has got to be borne in mind in the study of the financial machinery of the country.

The second important feature of the system follows

from the first and that is its unitary character. The Indian political system is unitary in the sense in which the term is understood by the students of Political Science. The Central and the Provincial Governments derive their political authority from the Secretary of State, and whatever power has not been specifically delegated by him remains in his hands. The different public authorities cannot claim any rights which they have not received from the Secretary of State in Council. This is the constitutional position and determines the financial arrangements of the country. They have not got any independent financial rights. The Secretary of State has, as a matter of expediency, been allowing greater latitude to the Governments in India in financial as in other matters. The Reforms, having been conceived with a view to give to the provinces a larger measure of independence of the Government of India, have brought about a further extension of this tendency, but the fundamental basis of the system has not been changed on that account. The Secretary of State is the repository of the financial authority, and the Central and the Provincial Governments have received their financial powers from him. He still continues to exercise general supervision in those spheres of financial administration, in which the authorities in India ordinarily enjoy a considerable liberty of action. The financial system of India, in all its details, embodies this central idea.

It has been said that the besetting sin of the Indian Government is their apotheosis of Efficiency with a capital E. The deeper and the wider significance of events is lost sight of in their desire to achieve technical perfection. This weakness of our administrative system may be admitted, but the very fact of admission draws our attention to another important feature of the system. It is *par excellence* an efficient system. It has got many faults, but according to its standard of goodness it works well. It may not prevent waste, it may have even undesirable effects on the economic welfare of the people, it may prevent

the realization of popular aspirations and reforms, but it does not allow or condone any irregularity. Those who are working it, insist on conformity to the regulations. The codes in which the regulations have been collected are bulky and voluminous, and the multiplicity of rules is sometimes found embarrassing by the financial experts themselves, but the tradition of regularity which has been built up in the transaction of the financial business is an asset of very great value, and has to be preserved. As a mechanism for the purpose for which it is designed, our financial system, in spite of its shortcomings, is quite effective. In the conduct of the complex business of national finance it is of very great importance that the unbusiness-like methods should be scrupulously avoided. It is possible that the adherence to this principle may mean delay in the carrying out of certain measures of reform, they may even at times stand in their way, but the slipshod methods of doing financial business leads to confusion in all spheres of national economy and have far-reaching effects on the soundness of public life. In receiving the heritage of the past, the future financial reformers may at times have to make use of their pruning knife, but they will not, it may be hoped, do anything to weaken the tradition of regularity which has been built with a considerable amount of labour and thought.

There is another characteristic of our financial system which deserves notice at this stage of our study. The system, besides being unitary, is a unified and co-ordinated whole. This is partly due to centralization which has, since 1833, been the outstanding characteristic of the administrative system. But its unity is mainly due to the desire of the authorities to keep the financial situation always in hand, and work out a policy through the financial mechanism. Lack of cohesion in the working of the financial system always leads to confusion, and makes it extremely difficult to have anything like a complete view of the national finances. The American system, which is a model of what a financial system should not be, is so unsatis-

factory on account of the absence of co-ordination. The methods of handling the public purse in the United States of America, which have been characterized by a student of public finance in America as "the most democratic as well as the most vicious"[1] have their origin in the political theory of the separation of powers. They have made the financial system unstable, and given to it the characteristics which, but for the immense economic resources of America, would have paralysed the whole system of administration. The Indian system does not suffer from this defect. The financial operations of India can be comprehended in their relation to one another, the meaning of the various proposals of revenue and expenditure understood with reference to the annual scheme of finance; and it is possible to trace the elaboration of a policy in financial acts of the executive authorities. At all stages of the execution of the policy a sense of unity is always kept alive, and the system works in such a way as to enable those who are in charge of it to keep their finger on the financial pulse of the nation, and satisfy themselves that there is nothing amiss. The significance of this point will become clearer in the later chapters of the book. Here it is enough to mention that the different parts of the system are well co-ordinated, the financial responsibility in the management of the central and the provincial finances is centralized, and the smooth working of the system, without any friction or overlapping, fairly well assured.

The financial system of the country, like the country itself, is passing through a period of transition. The features referred to above have to be kept in mind in the study of the system in order to get an intelligent idea of its working. But the new forces are at work, and the edges of the system are being worn off a little. The changes are not sufficiently important to change its essential character, but they are coming. It is desirable to know what they are and how they are affecting its working. As the new order emerges, the outlines of the system will, to a certain

[1] *Vide* Collins, "National Budget System and American Finance," p. 97.

extent, be blurred over in the process. The next step in our study must, therefore, be to take these new factors into account, and understand the national impulses which have brought them into being.

The new political system which was established in 1919 was based on the duality of control. The Executive of the provinces is subject to two authorities, and even in the Central Government, in which the element of responsibility has not been introduced, the juxtaposition of two distinct and, in certain respects, divergent factors is a fact to be reckoned with. A beginning has been made in the direction of establishing popular control and accounts for the introduction of many devices which have been adopted to enable the popular element to affect and influence, if not determine, the financial policy of the country. There is a difference of opinion regarding the wisdom of this step, but for our purpose the existence of this fact is of some importance. The financial system till now has been based on certain assumptions, which have been partially modified by the recent constitutional changes. The authority of the Secretary of State as the final arbiter of India's financial destiny has been tampered to a certain extent, and though he still possesses the constitutional right of asserting his will over the whole domain of the financial administration, the exercise of this right is in practice subject to practical limitations. The reality and the strength of these limitations depend upon a number of incalculable factors, but it may be taken for granted that they do exist. The British Government and the Government of India are still supposed to be the custodians of "welfare and the advancement of the Indian people," and the Secretary of State as the agent of one and the chief of the other is the highest authority. His absolute power, however, is diluted by a mild admixture of the financial powers of the Reformed Legislatures.

The ultimate future of the Indian constitution neither has been nor can be defined. The authors of the Joint Report have envisaged to themselves the India of the

future "as a sisterhood of states, self-governing in all matters of provincial and local interests. . . . Over this congeries will preside the Central Government dealing with matters, both external and internal, of common interest to the whole of India."[1] This is a good picture of India's future as far as it goes, but it does not go far enough. It is not quite clear as to how the Central and the Provincial Governments will share among themselves the ultimate political authority. Their financial relations will bear a close relation to their administrative relations, and the latter being indefinite, the former necessarily remain vague in their vision of the future. But our immediate problem is less complex, and it is not necessary for its solution to raise these important issues. On account of the vastness of provincial areas and the importance of provincial interests, it is necessary to give to the provinces a large measure of financial as well as administrative independence. The problem is not new, and has, since Lord Mayo's time, been receiving the attention of the Indian rulers from time to time. The present position is the outcome of a number of measures which had as their object the grant of wider opportunities to the provinces to have their own financial policy suited to the local requirements. The Reforms have been introduced with the avowed purpose of carrying further what is known as the financial devolution. The financial system, though essentially unitary, is not as compact as before, and makes it possible for the provinces to have, not the independent financial rights for the exercise of which they need not render any account to any outside authority, but a certain measure of financial autonomy. The arrangements bear on their face their transitional character, and cannot find an abiding place in our financial system. But they introduce a new element in our financial organization, which is capable of further development. It has a great potential value.

The financial system has been and is still dominated by considerations of administrative efficiency, and has, as

[1] *Vide* Montagu-Chelmsford Report, para. 349.

already remarked, realised it in a considerable degree. But the ascendancy of the purpose is being modified by certain other factors. The need for developing a sense of responsibility among the subordinate financial authorities has been recognized, and some attempt has been made to satisfy it. It has been also admitted that the financial system of the country should attach due weight to the local sentiments and traditions, and the Decentralization Commission[1] of 1907 urged this consideration among others as an object worthy of attention. Of late the importance of finding scope for the expression of democratic forces has received more attention and inspired the recent constitutional changes. It is a law of being of all organisms, including the political, that the functions determine the character of the organs. A change in the purpose or purposes which the system is intended to fulfil must, as a matter of necessity, lead to corresponding changes in the financial organization. The new purposes have, in order to count in the working of the system, to make their way through a mass of practices which have outlived their utility. The process must, therefore, be slow, and be accompanied by a radical change in the outlook of those who have to implement the new ideas into the existing system. The change is coming and will be quickened by the march of events in other spheres of national life. It may be hoped that it will not be carried out in a way as to place the purposes of efficiency and regularity at a discount, for undesirable as it is to make them unduly predominant it is highly desirable to keep them in view, and make them important factors in the management of the national finances. An inefficient system can do no good, whatever be the nature of the aims which we may seek to realize through it. But it is not necessary to labour this

[1] The Decentralization Commission referred to here was appointed in 1907 by Royal Warrant to enquire into the relations existing between the Central and the Provincial Governments and suggest measure of decentralization for introducing a system better adapted to meet the requirements and promote the welfare of different provinces without in any way impairing its strength and unity. Mr. C. E. H. Hobhouse was the chairman of the Commission and Mr. R. C. Dutt one of the members.

point, as it is very unlikely that there will be any sudden deterioration in the system. What is necessary for us to note is that the financial system of India is in a state of flux and the new impulses of national life are trying to express themselves through it.

The unity and symmetry of the system have to be preserved in spite of the dynamic nature of the forces which are working changes in all departments of national life. The co-ordination of the various parts which, as it has been observed already, is such a wholesome feature of our financial system, should not make it rigid, for rigidity will hamper national growth, and make new adjustments very difficult. There are certain progressive impulses in the country which are causing the financial system to be put to unaccustomed uses. Those who have acquired certain habits of thought on the assumption that the present system is to remain intact, are likely to find the impact of the new tendencies a little embarrassing. But it should be understood that the new forces are at work, and make the assumption of a static order of things untrue to facts of life. It will be a misfortune if these forces upset the financial arrangement to the extent of making their general co-ordination less satisfactory than it is at present. But the consideration of cohesion cannot override the need for making the system flexible enough to give free play to these vital factors. The system, while retaining its unified character, is to be a means, among others, of realizing the constantly expanding national life. All this is a little vague, but has a very important bearing on the working of the financial system and its future development.

There is one characteristic of our system which has to be referred to in passing before this introductory chapter is brought to a close. It has been recognized by the students of the financial systems, that the system which has been in existence in England for over two hundred years and has, like her national liberty, broadened down from precedent to precedent, exercised a very important influence on the financial systems of various European and Asiatic

countries. In each country there are, of course, certain variations due to the difference in the form of government and the national peculiarities, but the influence of the English financial system has been great on account of its intrinsic superiority. The Indian system, for obvious reasons, bears the traces of the influence of the same system. The intimate contact of India with England and the subordinate position in which she is placed with regard to the latter have made our financial system particularly susceptible to the influence of the English system. Her finance members, from Wilson downwards, have been men either directly recruited from England and had in most cases the experience of the English Treasury, or they were members of the Indian Civil Service, who looked up to the English financial system with filial reverence, and took it as a model of perfection. Sir David Barbour, an ex-Finance Member of India, spoke for all his predecessors and successors when he said in his evidence before the Welby Commission[1] "We take our principles of finance from England."[2] The resemblance between the Indian and the English systems is a very striking feature of the former, though in certain respects the two are very much unlike each other. The cardinal point of difference is due to the difference in the political systems of the two countries. In England the absolute control of the Parliament is the dominant characteristic of her financial system and is the key to its understanding. In India the constitutional function of the financial system is or at least has not been very important, and the constitutional safeguards and

[1] The Welby Commission referred to here and in the subsequent chapters was appointed in 1895 by Royal Warrant to enquire into the administration and management of expenditure chargeable to the Indian revenues and the apportionment of charge between the Governments of the United Kingdom and of India. It submitted its report in 1900. The Report of the Commission and its appendices are a veritable mine of information on all matters pertaining to the Indian finances. Sir W. Wedderburn, Messrs. Caine, and Dadabhai Naoroji wrote a separate report in which the Indian point of view was presented with very great ability.

The Commission is known after the name of its chairman, Lord Welby.

[2] *Vide* Welby Commission Report, Vol. III, para. 2039.

checks, though non-existent, have not had any important effect on its development. The fundamental difference makes the resemblance between the two systems which is otherwise very striking, somewhat superficial. It exists as far as the technique of the system is concerned, but the informing spirit in each case is different, and it brings home to our mind the fact that while one country is the home of freedom, the other has still to win it. This is not the only difference between the two systems. There are others which will, in due course, receive our attention. But the resemblance between the two systems, whatever it is, has some significance. India has got a financial system which is modelled on another, the distinguishing characteristic of which is the combination of complete popular control with a high standard of efficiency, and as she advances on the path of political freedom, she will find a financial system already in working order which, with some modifications, can become a suitable instrument for realizing the efficacy of the democratic control. The change will not be automatic. It will require the pursuance of a purpose deliberately set before the nation. But the task of reconstruction, if properly carried out, will not require the complete overhauling of the present system. The English system is the most perfect system known to the students of finance, and has, for reasons not of our making, been a potent factor in the development of our system. The Finance Members who have left a personal impress on our financial administration were, as already stated, men for whom the English system was a source of inspiration; and they have, as far as possible, adhered to the English model in working out the financial arrangements of this country. This consideration should have a moderating effect on our zeal for having a financial system suited to our traditions and environments. It is not that we should merely transplant to our soil a system which has thriven on another, but that we should proceed very cautiously, and, as far as possible, incorporate in the present systems the changes which may be necessary from the

national point of view. It should be possible to carry out these changes without neutralizing the influence of the English system unless there are some compelling reasons for doing so.

The plan of the book is simple, and can be understood by having a look at the table of contents. The next chapter gives an account of the financial structure as a whole. In the third and fourth chapters, the principles and methods of the preparation of the estimates and of the legislative action with regard to them have been explained. The fifth chapter is a brief study of the difficult question of the fiscal relations of the Central and Provincial Governments; in the sixth, the details of assessment and collection of revenue; in the seventh, of their expenditure; in the eighth of the receipt, custody, and issue of public funds; in the ninth, the maintenance of the balances and their distribution, have been set forth in order to give an insight into the career of estimates after they have been disposed of by the Legislatures. The tenth and eleventh chapters contain an account of the system of accounts and audit, and the twelfth and thirteenth of the administration of public debt and local finance. In the last chapter the leading principles have been summarized and the need of understanding them emphasized. The book is to be read as a whole as it is not possible to understand the arguments of individual chapters without knowing what has been said in the preceding chapters.

NOTE.—The remarks regarding the American Financial System in this chapter and other chapters of the book have to be read with some reservations in view of the changes introduced by the American Budget and Accounting Act, 1921. This measure is a very important landmark in the financial history of America, and is likely to give her a much more efficient and sound system of financial administration than she has had for a very long time. The most important change introduced by it is the creation of a Bureau of Budget in the Treasury Department which has been invested with the "authority to assemble, correlate, revise, reduce, or increase the estimates of several departments and estimates"; and it has been definitely laid down in the Act that no "estimate or request for any appropriation and no request for an increase in any item of any such estimate or request and no recommendation as to how the revenue needs of the Government shall be met shall be submitted to Congress or to any committee thereof by any officer or employee of any department or establishment unless at the request of either House of The Congress." These provisions will centralize financial responsibility, and if the Congress abstains from exercising financial initiative, the American financial system will, in due course, wipe off the stigma of being one of the most corrupt and inefficient systems known to the students of finance. This will, however, take time. In financial matters traditions count for more than anything else, and America has a big legacy of the most pernicious traditions to work off in order to attain a high standard of efficiency and purity in financial administration.

CHAPTER II

FINANCIAL STRUCTURE

India Office.—The financial administration of India is carried on from three centres. The first is the India Office. As the supreme authority over the administration of revenue and expenditure is vested in the Secretary of State in Council, by the Act of the Parliament, it is important to know the financial constitution of the India Office. A committee of the India Council, assisted by the Finance Department of the India Office, is the financial adviser to the Secretary of State in Council. It is charged with the duty of considering and examining all proposals involving fresh expenditure whether initiated in England or in India. All questions of increase or decrease of taxation and others even indirectly touching the finances of the country are considered by it before they are referred by the Secretary of State to the Council for its decision. The Finance Department of the India Office, besides controlling and directing the expenditure in England, considers and criticizes proposals of expenditure received from India which, according to rules framed under the Act, require the sanction of the Secretary of State in Council. All financial reports and returns received from India are carefully examined by the Finance Department. From the Finance Department to the Finance Committee and from the Finance Committee to the India Council is the procedure for transacting all financial business of the India Office. The decision of the Secretary of State in Council is final in all financial matters, and the possibility of its being questioned by the Parliament is so very remote that it need not be taken into account for all practical purposes.

There are two other officers in England, who are also intimately connected with the transaction of the financial business of India in that country. The Accountant-General is the head of the department, which is independent of the Finance Department of the India Office, and is concerned with the preparation of accounts, the management of cash balances, including the question of the temporary investment and examination of all claims and payments of all sums on behalf of India. The other officer is the Auditor. The duties of the Auditor have been defined by the Government of India Act as the examination and the audit of the accounts of receipts, expenditure, and disposal in the United Kingdom of all money, stores, and property applicable for purposes specified in the Act. He has got the power to call for any information relating to the accounts in the United Kingdom, and summon and examine any officers in relation to such accounts. He reports to the Secretary of State in Council his approval or disapproval of these accounts with such remarks as he may think fit to make. It is part of his duty to take special note in his report of any case in which it should appear to him that "any money arising out of the revenues of India has been applied to purposes other than those to which it is applicable." It has been provided for in the Act that all such reports should be laid before both the Houses of the Parliament together with such accounts to which they relate.

Finance Member.—In India the ultimate control of the finances rests with the Governor-General in Council. He is advised in all financial matters by the Finance Member of the Council, who, with the assistance of the Finance Secretary, is responsible for the sound administration of Indian finances. There is a difference of opinion about the position and powers of the Finance Member. There are some who hold that he possesses adequate powers to secure the consideration of the financial aspect of all public policies, and can, if he has got the will and personality,

make financial considerations tell. He, according to this view, has sufficient authority to exercise an effective control over the financial administration of the country. The other view is that whatever be his powers in theory, their use, in actual practice, is subject to important limitations. They first point to the predominant position of the Viceroy in the Indian constitution. The support of the Viceroy matters for every department of the Government of India, but the prospect of the considerations of economy and the taxable capacity of the Indian people being taken into account in connection with a proposal brought forward by any administrative department depends entirely upon the view that the Viceroy takes of the matter. The Viceroy's Council is, in theory, collectively responsible for the general administration of the country. The members of the Council are expected to look at the matters brought before the Council from a comprehensive standpoint, and not merely as the heads of the respective departments. But on account of tendencies inherent in a system of government like ours and the comparative absence of effective popular control, the financial aspect of the public policies is, quite often, likely to be relegated to the background in the deliberations of the Viceroy's Council, and the need, real or assumed, of giving effect to a particular policy carry the day. The Finance Member, in his speech in the Legislative Assembly in connection with the Budget of 1921–22, spoke of the change which had taken place in the financial powers of the Indian Legislature on account of the Reforms and exhorted the members to realize that they, in future, would have to share his responsibility in all financial matters. The financial powers of the Indian Legislature need not be considered here, but it may be stated that with the Finance Member still rests the responsibility of drawing the attention of the Viceroy's Council to the importance of counting the cost of their pet schemes and policies, and in the performance of this thankless task he, unlike the British Chancellor of Exchequer, cannot reinforce his arguments in favour of economy by pointing

to the necessity of justifying a costly policy to the Indian Legislature and obtaining its consent. The Finance Member, as Mr. Gokhale once said, is the only member interested in economy, and for want of support from any other quarter, is likely to follow the line of least resistance, and relax his insistence on considerations which, he knows from experience, do not receive sympathetic treatment. The Finance Member is further handicapped, because he is, at times, required to find money for policies initiated and matured by the India Office. It is possible that the Government of India may be consulted by the Secretary of State before these measures assume a definite form, but on account of the constitutional relations of the two authorities and the distance separating them, it is very unlikely that the Finance Member should be able to affect them in the light of his own knowledge and experience. The Finance Member is generally called the Indian Chancellor of Exchequer, but he has not got behind him that weight of tradition and the control of legislature which enables his English prototype to be such a potent factor in the financial administration of the United Kingdom. The Chancellor of Exchequer controls the expenditure of his colleagues, while the Finance Member in India has, in a number of cases, merely to register it.[1] He has, to use the words of Mr. Eardely Norton, "to arrange the mosaic not of his own making in a respectable pattern that shall please the eye." He is, however, the financial adviser of the Government of India, and represents in his person the

[1] The difference between the functions of the Finance Member and the Chancellor of Exchequer is brought out in an answer given by Sir David Barbour in his evidence before the Welby Commission:

Q. 1828.—In other countries, the Finance Minister is rather a Registrar than the Controller of expenditure of his colleagues. May I take it that your opinion inclines to the view that the Indian Finance Minister's powers resemble those of our Chancellor of Exchequer than those which I attribute to the foreign Ministers of Finance?

A.—Well, theoretically, they more closely resemble the powers of the Chancellor of Exchequer, but practically and at times he might be much more in the position of registering the expenditure which other authorities wish to incur than that of actually controlling it.—*Vide* Welby Commission Report, Vol. III, paras. 1827–8.

highest financial experience and wisdom that is available in this country.

Finance Department.—The Finance Department of the Government of India, over which the Finance Member presides, exercises two-fold functions. It performs administrative duties in financial matters arising out of the spheres of work, which are under the direct control of the Government of India. It is in charge of the monetary and banking systems of the country. It scrutinizes all proposals for fresh expenditure, and prepares a forecast of revenue and expenditure of the Government of India. It watches the progress of income and expenditure and ascertains the rate at which it is proceeding. It re-assures itself, from time to time, that the whole financial system of the country is in a sound condition. It can generally take steps to meet any unforseen development that may appear on the financial horizon. It is, in one word, the central station from which the network of financial operations is regulated and kept working in an efficient manner. It may, however, be mentioned that a separate branch, styled as the Military Finance Branch, has been constituted to deal with the questions relating to the military finances of the country. An officer of the Finance Department, known as the Financial Adviser Military Finance, is in charge of the Military Finance Branch. He acts in a dual capacity. He is on one hand, the representative of the Finance Department of the Army Head-quarters and, on the other hand, an expert adviser of the Commander-in-Chief and his Staff in all matters of Military Finance and expenditure. He is a member of the Army Council. He is to prevent irregularity in expenditure, ensure the observance of the financial principles, and also assist the Commander-in-Chief in the financial administration of army services. He works under the direct guidance of the Finance Member, and in all important matters takes his instructions. The other function of the Finance Department is supervisory. The Reforms have decreased the importance of this function, and every advance in the

constitutional development of the country will lessen the need and the occasions for the exercise of this function. But this part of the work of the Finance Department still is, and will for some time to come, continue to be of some importance. In this capacity it supervises the administrative work of the different provincial finance departments. All applications for incurring expenditure which the Provincial Governments cannot sanction on their own authority, are submitted for the sanction of the Secretary of State in Council through this department. Under the Reforms the need of what the Court of Directors called "petty, vexatious, meddling interference" has ceased; the Provincial Governments have been given wide financial powers, and are not subject to the detailed control of the Finance Department of the Government of India. But the disappearance of all control by the latter will depend upon their getting full autonomy in internal matters. The Finance Department has still to keep a watch over the provincial finance.

Revenue Department.—The Revenue Department of the Government of India, though not directly connected with the financial organization of India, performs functions, which have financial significance. Once the most important source of Indian revenue, the Land Revenue even now, in spite of the growing importance of Customs and Income-tax, occupies a very important place in our fiscal system, and is the mainstay of provincial finance. The Revenue Department is in charge of the administration of Land Revenue, and the Revenue Member, though he does not belong to the hierarchy of the finance officials, is, by virtue of the duties which he performs, an important functionary in our financial system.

Auditor-General.—The officer next in importance to the Finance Member is the Auditor-General. His duties fall under two heads, viz. audit and accounts. He was before the Reforms an officer of the Indian Finance Department, and held his office on the same terms as the other public

servants. But now, on account of the importance of his duties, his status has been raised. He has been made a statutory officer, and, as the Chief Auditor of the State, is independent of the Government of India. The actual audit of accounts is either done by officers directly under his control, or by officers of the various departmental audit offices who, though independent of him for administrative purposes, do their work under his general surveillance. He is the final audit authority in all doubtful and disputed cases, and is responsible for efficiency of the audit of expenditure in India. He arranges for the inspection of the work of the various audit officers through his two assistants, styled as the Deputy Auditors-General. These officers visit the different centres of accounts in order to satisfy the Auditor-General that the detailed audit conducted by the local and departmental officers is efficient, that the regulations and the orders of the Government are duly observed, and the procedure in force in those offices is suitable for the efficient discharge of the audit and accounts duties. The Auditor-General can, in this way, enforce a high standard of efficiency in the audit of the Government accounts, and bring to bear experience of one office to suggest improvements in the work of the other. He receives from the audit officers the reports reviewing the results of audit conducted by them during the past financial year, and transmits them to the Secretary of State with his own remarks. The accounts duties of the Auditor-General are equally important. He prescribes the form in which the accounts are to be kept, and rendered by the accounts officers. The different heads under which the financial transactions are to be grouped are to be laid down by him, and in case of a difference of opinion as to the right head under which a particular transaction should fall, the matter has to be referred to him for his decision. He compiles the annual accounts of the whole country and submits them to the Secretary of State in the form prescribed by the latter. The combination of audit and account functions has been taken exception to on various grounds, and their

separation advocated for making the audit in India more efficient and independent.

Military Accountant-General.—The military finance, as already remarked, has on account of its size and importance an organization of its own in the Central Government. The Military Accountant-General is the head of the accounts branch of the Military Department. He is not an audit officer in the ordinary sense of the word, as he does not conduct or review the audit of accounts. But he receives reference on questions, which raise points of principle or are not covered by regulations. He is responsible for the orderly conduct of the work of the Military Accounts Offices, and receives a number of reports, which enable him to exercise a general supervision. He has an officer under him, whose main duty is to visit and inspect various Military Accounts Offices and submit a report on the work done by them. He consolidates the reports on the results of audit of the military accounts prepared by the audit officers and sends a combined report to the Auditor-General. He is under the administrative control of the Finance Department and has to work under the orders of the Financial Adviser Military Finance.

The Controller of Currency.—The Controller of Currency performs four duties. He, to use the official language, is in charge of the currency, resource, ways and means operations of the Government of India, and the management of public debt. His currency functions make him responsible for the working of the Indian currency system, the custody of the securities and cash held in India as a part of the currency reserve, the adequacy of the currency balances and their distribution among different treasuries and paying centres. The resource operations are undertaken to keep sufficient funds at each paying centre to make all Government payments, without unnecessary locking-up of funds in any one of them. The "ways and means" is a technical phrase used for the arrangements "by which the cash balances of the Government, including the portion held in England, are so regulated as to assure

that they shall at all times during the year be sufficient to meet the demands made on them in India and in England. Into these balances enter not only multifarious sums due to and by the Government, which are generally known as the revenue and expenditure, but also very large amounts borrowed by Government for capital expenditure for railway and irrigation, and also other amounts in regard to which Government acts as a banker or a remitter, borrower or lender. . . . The whole of these enter and leave the treasuries and affect the public cash balances, and are technically known as the receipts and disbursements or incomings and outgoings as distinguished from public revenue and expenditure proper. A forecast of opening balances of the year and of the monthly incomings and outgoings is prepared; it is arranged, by adjusting the one to the other, by raising a loan, for example, or reducing expenditure that the estimated Government balances should never fall unduly low." This somewhat long extract from Sir F. Gaunlet's Introduction to Government Accounts has been quoted to give some ideas of the nature of ways and means operations, for the conduct of which the Controller of Currency is responsible. He is the watchdog of the public purse, focusses the accounts of income and expenditure of the whole country from month to month, and keeps the Finance Department informed as to the exact state of public treasury. The Controller of Currency is the link between the Government and commercial finance, and has to study the effect of one on the other. He has to avoid the conduct of financial operations in a way which might adversely affect the commercial finance. For the discharge of his duties he requires an intimate knowledge of the currents of trade and commerce, and other facts of economic life. The ebb and flow of trade and other movements of economic life have their repercussions on the receipts and disbursements of the public treasuries; and if he, as the signalman of the Indian finances, is to prepare the Government for the coming events, he must keep himself in touch with the fluctuations of economic

life and take prompt action when things take an unexpected turn. The solvency of the Government of India depends upon the satisfactory discharge of the duties assigned to the Controller of Currency. He is directly under the Finance Department.

Provincial Financial Machinery.—The Provincial Governments taken together are the third agency for the financial administration of the country. Each Provincial Government is the unit for the financial business of the province over which it exercises administrative authority. The financial powers which it possesses have been delegated to it by the Secretary of State and are exercised under the general supervision of the Government of India. They are, in the major provinces, vested in the Governor in Council. His chief adviser in financial matters is the Finance Member of his Council, who in many respects performs duties analogous to those which are discharged by the Finance Member of the Central Government. He presides over the Provincial Finance Department which is "a microcosm of the central finance organization." With the creation of two final authorities for the preparation of the proposals of expenditure and their sanction, the provincial finance has become a very complex and delicate arrangement. The duty of the Finance Department is to maintain a high standard of financial probity and secure a full consideration of the financial aspect of the public policies. All proposals for expenditure and changes in taxation are examined by it before they are inserted in the financial programme of the year. Though it cannot veto or override the decision of the Governor in Council or Ministers, it can insist on being consulted on the financial provisions of the public policies, whether proposed by the Reserved or the Transferred half of the Provincial Government. It, like the Finance Department of the Government of India, prepares a forecast of revenue and of expenditure, and keeps a watch over the financial business of the province. The position of the Finance Member, after what has been said about the Finance Department, does not call for any explanation.

It is very difficult under the present constitution, on account of the fact that both halves of the Provincial Government have to dip into the same purse. With the duality of control within the province and a certain measure of supervision of the Government of India, he is likely to find himself handicapped in more ways than one in evolving anything like a financial policy of his own. He can put things in shape, ensure the orderly conduct of financial business, and prevent waste in public expenditure, but he cannot have, on account of the limitation under which he has to work, a stable, consistent, and well-conceived financial programme of the province.

Accountant-General.—The Accountant-General in the province is the officer of the Central Government, and is charged with the duty of maintaining and auditing the accounts of civil expenditure, both Central and Provincial. The Government of India counts upon him for maintaining a high standard of efficiency in the administration of provincial finance, and bring any infringement of what are called canons of financial propriety to the notice of the superior authorities. It is his duty to prevent any changes in the main structure of accounts and keep a watch over the financial business of the province. He is responsible for the initial audit of accounts and for pointing out the limits within which the Provincial Governments have to exercise their financial powers. He assists the Provincial Governments in preparing its financial forecast, and is bound to supply any information that it may require for the discharge of its financial responsibility. He has been aptly called the ambassador of the Central Finance Department in the province, inasmuch as he is expected to insist on the observance of general principles of financial administration, and exercises a supervision on behalf of the Government of India and the Secretary of State over the financial methods and policy of the Provincial Government. While recognizing the eventual necessity of constituting separate provincial accounts officers, the Government of India are of opinion that the Accountant-General should, during

the period of transition, remain under the absolute control of the Central Government, and carry on his duties in complete independence of the Governor in Council, and the Ministers. The future position of the Accountant-General will be determined by the constitutional relations of the Central and Provincial Governments. They are, at present, the link by which the Central Government binds the Provincial Governments to itself in matters of financial procedure and policy; and provides against the introduction of wrong and unbusiness-like methods in the conduct of provincial finance. It may be added that the Accountants-General are under the Auditor-General in all audit, accounts, and administrative matters.

Deputy Controller of Currency.—In all provinces, except Madras and Burma, there are Deputy Controllers of Currency. They are the assistants of the Controller of Currency, watch the progress of receipts and expenditure and regulate the transfer of funds from treasuries which have more than enough to others that have not got enough for making the Government payments. They, like the Accountants-General, are not provincial officers, but the smooth working of the provincial financial machinery depends a great deal upon the efficiency and promptness with which they do their work. In Burma and Madras the Accountants-General are the ex officio Deputy Controllers of Currency, and carry out their duties, in that capacity, under the orders of the Controller of Currency.

Treasury Officers.—All payments, whether on behalf of the Central or Provincial Governments, are made by the Treasury Officers, who also receive all monies which are paid to the various officers in their official capacity. They are assistants of the district officers, but act under the orders of the Deputy Controller of Currency. They are responsible for the safe custody of Government funds, and have to keep correct accounts of the Government receipts and payments. They inform the Deputy Controllers of Currency of the probable receipts and expenditure before they actually occur in order to make it possible

for him to bring about an economical and proper distribution of funds. They are the paymasters of the Government.

This account of the financial structure will, it is hoped, give some idea of the vastness of financial operations and solidarity of the system. From the Treasury Officer to the Secretary of State in Council, the whole system possesses a unity of purpose ; and its integrity and symmetry, in its conception and actual working, make it an entire whole, each part of which has a place and significance of its own. The Government officers have generally a tendency of looking upon themselves as cogs of a big machine and often lose sight of the underlying principles. The finance officers of the Indian Government can, if they so choose, perform their duties with reference to the whole of which they are the parts, and understand their place in the financial organization.

Having explained the principal features of the financial organization, we are now in a position to begin the study of its actual working. In the financial business of the State, foresight is a cardinal virtue, and every well-administered State, in exercise of this quality, calculates what expenses it will have to meet during the ensuing financial year, and makes plans to meet them. It takes stock of the existing financial situation, tries to interpret the meaning of the tendencies that may be at work in the light of its past experience, and anticipates future developments on the basis of ascertained administrative policy and the likely occurrences of the coming year. This forecast of expenditure and income is the first financial act of the Indian Government, taking the financial year as the unit of our study. An explanation of the aims and methods which govern the preparation of this forecast, technically known as the estimates, is the object of the next chapter.

CHAPTER III

PREPARATION OF ESTIMATES

THE importance of the preparation of estimates for the satisfactory management of public finance cannot be exaggerated. In the initial stages the estimates are in a very plastic condition, and can be drawn up with a view to give effect to a policy or carry out a programme. Their preparation is not merely a matter of arithmetical calculation. It requires the combination of ripe experience, technical knowledge, sagacity, and sound judgment. It is not simply a compilation of the figures furnished by the different Government officials. The tendency inherent in all Government departments to take the *status quo* as the norm to which the official activities should conform and work up to, is particularly strong in the financial administration on account of the inconvenience of introducing a new element in the transaction of a highly complex business. But the mechanical repetition of the figures of the past years cannot serve any useful purpose. In order to guard against this besetting weakness of all official systems, the British Treasury issues annually a stereotyped admonition to all officers connected with the preparation of the estimates warning them against assuming the last year's estimates as the starting-point for those of the next. In the Civil Account Code, which is, as is well known, the Book of Wisdom for all officers connected with the administration of Indian finance, there is a standing instruction to the effect that the undue amount of reliance should not be placed on the figures of the past years. There is nothing easier than to take the last year's estimates for granted, adding something to every item for which additional

expenditure can be foreseen, but it is wrong in principle to follow this method in the preparation of the estimates. The estimates of expenditure, if they are to be of any value, should be based on the anticipations of the coming year and not on the facts of the current one. The forecast of expenditure is, however, only a half of the estimates; the other, and a more important one, is the forecast of the public revenues. A correct estimate of income from the various sources of revenue can only be possible if it is based on the first-hand knowledge of the economic conditions, and an intelligent interpretation of the factors affecting the trade and industry of the nation. The State income being mainly derived from the social income, the magnitude of the latter, and its fluctuations, due to the working of the economic system or that of the world factors, are a matter of a very great importance, from the standpoint of the financier, who is trying to look ahead and know the secrets of the future. The art of preparing estimates, requiring technical skill and understanding of the nation's ability to pay, requires that the estimating officers should remain in contact with the movements of economic life, which, on account of its ever-growing complexity, are becoming more varied and frequent, and know their effect on the public revenues. The estimates are the corner-stone of every financial system, and the extent to which the anticipations correspond to the actual events, is the measure of the competence of the finance officers, and the efficiency of the system as a whole.

In preparation of the estimates certain objects have to be kept in view. The first and the most important is that they should be framed as a unit. The estimates for the various departments should be so drawn up and reviewed as to enable the financial helmsman of the country to have a financial programme. They should not be an aggregate of the estimates of the departments working independently of one another and pressing their needs without any reference to the financial policy of the year. All the proposals of the departmental expenditure should be con-

sidered in relation to one another, and fit in a balanced scheme of financial operations. They should embody a consistent and well-considered plan. The object next in importance to the need of having a financial policy is that the revenue and expenditure should be balanced and what are called the deficit budgets should, as a rule, be avoided. Under certain exceptional circumstances it may be permissible and even necessary to let the expenditure be in excess of the income ; but, in view of the serious consequences of doing so over a long period, a lack of equilibrium between the two sides of the estimates should always be viewed with very great concern, and promptly provided against. The excess of income over expenditure is also undesirable, and though it does not lead to the serious consequences comparable to those, which are known to ensue from the excess of expenditure over income, the estimates should, as far as possible, not err on the side of underestimating the income or over-estimating the expenditure of the State. The accumulation of the surpluses and swelling of the Treasury balances leads to public extravagance, and should, as Mr. Gokhale pointed out in his trenchant criticism of the Government policy years ago, be avoided either by the remission of taxation, or increase in expenditure on the material and intellectual betterment of the people. The estimates of revenue, therefore, should neither be over-optimistic nor conservative to a fault. It is not necessary to add the self-evident fact that the considerations of economy should be a very important factor in the framing of estimates. The consideration is as important as it is often neglected, but its paramount need is so obvious, that it is possible to overlook it just on that account. The form in which the estimates are prepared, and presented to the legislatures has also an importance of its own. It is determined by a number of considerations. The administrative organization of the State must necessarily have an important influence on its determination. The convenience of legislative study, and the passage of the budget

through the Legislature is another important factor, and calls for what Prof. Adams describes as a "compromise between financial and political interests." The expenditure must correspond to the various administrative needs of the State and bring together the proposed expenditure on a particular service under one head. They must be clear, simple, and easily understood. The classification should neither be so very comprehensive as to make it impossible for the Legislature to express its disapproval of particular financial proposals, nor so very minute as to make the study of estimates a bewildering pursuit. There is one more consideration with regard to estimates which has more than a book-keeping importance. The changes in the form of the estimates, once adopted after the consideration of the various aspects of the question, should not be made without really sufficient reasons. The frequent changes in the form of the estimates would introduce a great uncertainty and confusion in nations' accounts, make comparisons with the financial results of the preceding years extremely difficult, and enable the executive to elude vigilance of the legislature by introducing new charges under headings, the contents of which have, by customary use, acquired a particular significance. The work of examining the estimates, is, from the nature of things, a difficult undertaking, but the introduction of frequent changes would make it a hopeless pursuit. The changes, when and if unavoidable, should be duly announced, and their effect on the estimates brought into prominence to warn the public and the students of finance against drawing false inferences.

The time of the preparation of these estimates is also of importance, from the administrative as well as legislative points of view. It is, in the first place, highly desirable that very little time should intervene between the formulation of the financial proposals and their execution. There are certain items of expenditure which do not undergo any change with the lapse of time. The army expenditure in time of peace, and the expenditure on civil administration,

taking the scales of salary and allowances as fixed, do not undergo any change after the estimates have been once framed. But there are other important items of expenditure, the correct forecasts of which are subject to considerable variations on account of changes of prices and other facts of economic life. The estimates of the amounts necessary for the purchase of stores and provisions, for the execution of the projects of public works, for the construction of railways, for the grant of compensation for dearness and similar other charges cannot be made with any degree of confidence, if there is a long interval between their preparation and the commencement of the period, which they are intended to cover. The discrepancies between the estimates of revenue and the actual amounts realized are likely to be larger, if the fiscal laws come into operation long after the preparation of the estimates. The conditions of trade and industry are notoriously fickle, and any estimates based on the assumption of the stability of the economic conditions are likely to prove wide of the mark. There are other considerations which have to be taken into account in this connection. The estimates ought to be drawn at a time when the results of the financial laws of the previous year can be ascertained with a certain amount of accuracy. But the most important consideration which can be urged with regard to the commencement of the financial year is, that the estimates should be framed at a time when the important events of the economic life of the nation have declared themselves in order that their effects on the public receipts and expenditure may be ascertained, and provided for in the estimates. The selection of the date on which the financial year is to begin is, therefore, a detail of considerable importance, and has to be settled with a view to reconcile a number of considerations.

The considerations referred to in the preceding paragraph give us a convenient turning-point for explaining the methods of the preparation of the estimates in India. The dates on which the financial year begins in different

countries are, for obvious reasons, different. In India the financial year begins on the 1st April. It is difficult to find out why this date has been chosen. The first reason which suggests itself is that as in England the financial year begins on the 1st April, the same date has, on account of the insular ways of the Englishmen, been adopted in India to mark the beginning of the financial year. As Mr. (now Sir) B. N. Mittra put it in his evidence before the Chamberlain Commission, "They followed the practice in England, and having done so, they never gave serious thought to altering it." The other reason which can be suggested, is that as the Secretary of State, under the Government of India Act, has to lay before both Houses of Parliament in May the accounts of the Indian revenues and expenditure, it is desirable that the Government of India and the Provincial Governments should close their accounts early enough to enable the Secretary of State to fulfil his statutory obligation. Among other reasons given by Sir A. Colvin, an ex-Finance Member of India, in his evidence before the Welby Commission to justify the commencement of the financial year on the 1st April, are the desirability of the Viceroy's touring in the month of April before taking the summer residence at Simla, and the convenience of preparing the estimates before the end of March, when generally the English officers go to England on leave. Whatever may be the reason for the selection of this date, the need for the change in the financial year has been pointed out, on a number of occasions, on account of its unsuitability from various points of view. In 1864 and then again in 1873 the question was made the subject of official correspondence, but nothing came out of it. It was, later on, definitely raised by two Royal Commissions. The Welby Commission recommended the 1st January as the more suitable date on the ground that it was inconvenient to place before the public three statements: the estimates of the coming year, the probable actuals of the current year, and the completed account of the previous year—all of them relating to a single year's

accounts. "Financial statements," to use their words, "issued for the general use should be as simple as possible and a number of statements relating to the same period, but varying in their figures, no doubt tend to embarrass the public."[1] Fourteen years later the Chamberlain Commission[2] urged the necessity of the change for a still more conclusive reason. They emphasized the dependence of the Indian revenues on the success or failure of the agricultural operations, and the dependence of the latter on the monsoon, which, as is well known, spreads in India in the months of June to October. The Finance Member has, on account of the practice of presenting the estimates

[1] The defect referred to here is, however, due to the fact that the budgets in India are opened before the commencement of the next financial year. If the budgets were opened sometime after the 31st March, the actual results of the expired year would take the place of what are now called the Revised Estimates. These comprise the actual figures of revenue and expenditure of nine or ten months and the estimated ones of two or three. The figures in the Revised Estimates, which are now taken as the basis for ascertaining the financial results of the current year in the public discussion, show appreciable variations from the actuals. The Finance Member in his Budget speech of 1924 gave the figures of ten years to illustrate this point. The figures are given below :—

Table showing the actual Revenue and Expenditure of the Central Government as compared with the Revised Estimates from 1913–14 to 1922–23. (In thousands of rupees).

Year.	Revised Estimates.			Actuals.		
	Revenue.	Expendit're.	Surplus (+) Deficit (−)	Revenue.	Expendit're.	Surplus (+) Deficit (−)
1913–14	80,66,56	78,43,56	+2,23,00	81,32,71	77,85,85	+3,46,86
1914–15	74,89,38	79,07,25	−4,17,87	76,15,35	78,83,14	−2,67,79
1915–16	78,89,08	81,58,21	−2,69,13	80,00,96	81,79,26	−1,78,30
1916–17	97,25,67	88,27,37	+8,98,30	98,53,10	87,31,37	+11,21,73
1917–18	1,14,84,48	1,06,27,74	+8,56,74	1,18,70,58	1,06,57,52	+12,13,06
1918–19	1,27,94,65	1,34,79,88	−6,85,23	1,30,40,66	1,36,13,72	−5,73,06
1919–20	1,44,07,56	1,59,18,67	−15,11,11	1,37,13,98	1,60,79,27	−23,65,29
1920–21	1,35,10,35	1,48,03,61	−12,93,26	1,35,63,32	1,61,64,17	−26,00,85
1921–22	1,13,15,32	1,41,94,52	−28,79,20	1,15,21,50	1,42,86,52	−27,65,02
1922–23	1,20,70,17	1,37,95,52	−17,25,35	1,21,41,29	1,36,43,05	−15,01,76

It will be observed that the actuals, with the exception of two years, compare favourably with the revised estimates.

[2] The Chamberlain Commission referred to here is the Royal Commission on Indian Finance and Currency appointed in 1913 to enquire into various questions connected with the monetary system of India. The Commission recommended the adoption of the Gold Exchange Standard as a suitable system of currency for India.

before the end of March, to prepare them in ignorance of the most important factor on which the results of the year must depend. They said, "It is clear that from the financial point of view the present date is the most inconvenient possible, for the budget, and suggestion, therefore, has been made that the date of the financial year should be altered from the 1st April to 1st January or the 1st November." The highly speculative element of the Indian estimates is due to the fact that they are framed months before the significance of the most dominant event of the year is known. The Government have recently made the matter a subject of careful consideration, and have come to the conclusion that the proposal for the change of the financial year should be dropped.[1] In coming to the decision to which the Government of India have come, they have attached undue importance to the difficulties arising out of the recasting of accounts, and altering the various administrative arrangements. That there would be administrative difficulties in the change of the financial year was admitted by the Chamberlain Commission, but they recommended the change in the interest of accurate accounting and sound budgeting. There are no insuperable difficulties in the way of carrying out the reform. An extra intermediate budget will, of course, have to be prepared for effecting a transition from the old to the

[1] The decision of the Government of India is embodied in the Government of India Resolution, No. 83 F, dated the 18th January, 1923, which is reproduced below:

"The Government of India have had under consideration the question of changing the date of the commencement of the Indian financial year from the 1st April to the 1st November or 1st January. The matter has been raised on more than one occasion and notably by the Royal Commission on Indian Finance and Currency of 1913, the main object in view in advocating a change being that it would facilitate more accurate budgeting.

The opinions of the Provincial Governments and the Chambers of Commerce were invited on the proposal in a circular letter, which was also published in the Press. The replies show that the Provincial Governments are unanimously of opinion that the disadvantages which would result from the change would outweigh the advantages, while opinion among the commercial bodies is divided. After considering the matter in all its bearings, the Government of India have now decided to drop the proposal for a change."

new financial year, but the trouble of making it is not a very heavy price for introducing the more satisfactory arrangement. It is necessary to raise the issue again and settle it as early as possible.[1]

Home Estimates.—The Indian estimates are prepared by the three agencies responsible for the financial administration of the country. The estimates of expenditure incurred in England are prepared by the India Office and the High Commissioner for India. The India Office is responsible for the preparation of estimates of expenditure under the control of the Secretary of State in Council. The duties of the India Office have been classified by an official committee under three heads—political, administrative, and agency.[2] Under the new arrangements introduced by the Reforms the British Treasury is liable for expenses incurred in discharge of the administrative and political duties, and the cost of agency functions is charged to the Indian revenues. Under this arrangement the British Treasury pays the salary of the Secretary of State and Parliamentary Under-Secretary, and a grant-in-aid as its share of the cost of the maintenance of the India Office. The India Office prepares the estimates of the expenditure on general

[1] Since the above was written the question of the revision of the financial year has been raised again. The separation of railway finance from general finance has drawn attention to the unsuitability of the existing arrangements from the point of view of the railways. The Finance Member has expressed himself in favour of the change of the Railway financial year. The Railway Board in their Memorandum submitted to the Reforms Enquiry Committee have recommended the 1st of October as the date on which the Railway financial year ought to begin. They support these views with arguments similar to those given in the text. It appears that the question will soon be taken up again by the Government.

The Railway Board further urge that the Railway Budget should be introduced in the Assembly sometime after the commencement of the financial year in order that the figures of the actual receipts and expenditure of the last year may take the place of the revised estimates of the current year. A similar view has already been put forward with regard to the whole Indian Budget at the end of Chapter IV.

[2] Most of the functions have now been transferred to the High Commissioner for India. Agency work still remaining with the India Office relates mainly to subjects which are held to be intimately connected with the questions of policy and the issue of military leave, pay, and pension, the transfer of which has been postponed on account of the administrative difficulties to which it is likely to lead.

administration and the payments which it makes in England on behalf of the Government of India. The estimates are prepared by the Accountant-General on the basis of the information received from the various departments of the India Office, and submitted for the consideration of the Finance Committee and the Secretary of State in Council. The estimates, after they have received the final approval of the Secretary of State in Council, are sent to India with a despatch of the Secretary of State, and it is the practice to state the total amount of the sterling payments which are likely to fall due, and the mode in which the payments will be made. These estimates reach India early enough to enable the Government of India to take the anticipated payments of the Secretary of State into account before they frame their own estimates. But they are not subjected to any scrutiny by the Finance Department of the Government of India, and it would not be wrong to characterize their attitude towards these estimates as one of passive acquiescence. They are practically compiled into the financial statement of the Government of India without any examination whatsoever. The Government of India confine their comments, if any, to the mode of meeting sterling payments—that is, how far they are to be met out of the sale-proceeds of the Council Bills, how far by the issue of loans, or the use of some other method. The Secretary of State communicates by wire to the Government of India any corrections, if necessary, before the estimates are cast into final form.

The High Commissioner for India performs what are called the agency functions. He prepares the estimates of the expenditure on the maintenance of his establishment and of the amounts necessary for the purchase of stores and other payments which he has to make on behalf of the Government of India and the Provincial Governments. The estimates of expenditure on the purchase of stores and meeting other liabilities of the Indian Governments are prepared on the basis of information received from

India. The estimates of expenditure on the establishment and the purchase of stores, etc., for the Central Government are submitted by him to the Finance Department of the Government of India and examined by the latter. The estimates of the provincial expenditure are forwarded by him to the Finance Departments of the respective Provincial Governments, and included by them in their own detailed estimates after necessary examination. He also sends cables containing his final corrections to the estimates to the Governments concerned, before they are compiled.

The Secretary of State and the High Commissioner also prepare the estimates of their receipts, which are comparatively speaking unimportant, and include them in their consolidated estimates.

Central Estimates.—The estimates of the Government of India can be considered under four heads: Civil Estimates, Military Estimates, Estimates of the quasi-commercial Departments, and Revenue Estimates. The last may be taken first on account of their comparative simplicity.

Revenue Estimates.—The revenue estimates are prepared by the collecting officers, who are guided in their calculations of the anticipated yield of the taxes and other sources of public income by the figures of the previous years, but are expected not to reproduce the figures of the previous years mechanically. They have to take into account the prospective events of the coming year and make due allowance for their effect on the revenue-yielding capacity of the different sources of income. For the preparation of the correct estimates they require an intimate knowledge of statistical data of the previous years and the undercurrents of economic life, which, as already stated, have important significance for the amounts which are likely to accrue in the coming year. The estimates are prepared on the assumption that the current taxes and their rates will remain unchanged. The spending departments also prepare the estimates of the receipts which they get in

the course of the performance of their duties. The estimates are forwarded to the accounts officers with which the estimating officers have their dealings, who examine them with reference to their office records and other information available in their offices, and suggest any changes which, in their opinion, ought to be made in the light of the experience of the past years. The accounts officers submit the estimates to the finance departments of the Government of India. The Finance Department reviews them, and ascertains how far they are adequate to meet the expenditure which the Government has or wishes to incur in the coming year, and, if any changes are considered necessary, takes steps to have the modified estimates prepared in view of the proposed changes. The changes in taxation are, before they are embodied in the estimates, considered and approved by the Executive Council and sanctioned by the Secretary of State in Council.

There is one important rule which governs the preparation of all estimates of expenditure—central or provincial—which may be briefly referred to here, before the procedure for their preparation is explained. The rule is that no charge can be inserted in the estimates which has not received the previous sanction of the competent authority. The permanent charges are presumed to have been sanctioned already, and are not brought under the operation of this rule. But all important proposals for fresh expenditure require the sanction of the Secretary of State in Council or that of the Government of India or the Provincial Government concerned. In either case the Finance Department examines the proposals before they are submitted for the sanction of the authority competent to deal with them. The practice enables the Finance Department to exert its power of criticism before and not after the estimates have been submitted to it. Under this arrangement each charge is taken up and considered on its own merits under circumstances which give ample time for the due consideration of the proposed charge. The Finance Department considers it from the point of view of economy, and its

relative importance compared with similar proposals emanating from other departments and, of course, the limitations which the available resources impose on the financing of the new schemes are always kept in view. In the management of the financial affairs of the State it is of utmost importance that every proposal of expenditure should not only be considered on its own merits, but also in relation to all other proposals of expenditure. If the estimates are to be considered as a unit, and the balance between the total income and expenditure on one hand and among different objects of expenditure on the other is to be attained it is necessary that all proposals of expenditure should be considered from a broad standpoint. The British Treasury performs this function in a very efficient manner. The Finance Departments in India are expected to exercise the Treasury control, and give a unity to the working of the financial system. The objections urged by the Finance Departments may be set aside by the sanctioning authority, but the fact that the proposals are first examined by the Finance Department ensures that their financial aspect will receive due consideration in the formulation of the final decisions. The Finance Departments in India do not possess the amount of authority, which the British Treasury is known to exercise in the financial administration of the United Kingdom. That is due to causes which are intimately connected with the whole political constitution of India, and must continue to affect the practical utility of this rule. But the rule itself is salutary in its intent and effect, and the further constitutional changes will increase its utility.

Civil Estimates.—The civil estimates comprise all estimates except the estimates of the military, railways, and the post and telegraph departments. The preparation of the estimates begins with the submission by the lowest working units of the Government to their superior officers, known as the controlling officers, the estimates of their requirements for the ensuing year, generally in August

of the year preceding that to which they relate. They are submitted on the prescribed forms. The controlling officers forward these estimates to the head of the department with an explanatory note if necessary. The head of the department consolidates them, and sends one copy to the Accountant-General, Central Revenues, or the Provincial Accountant-General as the case may be. The Accountant-General examines these estimates to see that no unauthorized charge has been inserted therein, all variations from the figures of the previous years have been duly explained, and otherwise the estimates are in order. The examination by the Accountant-General is a formal affair. He is not concerned with the policy or the questions relating to the advisability or otherwise of expenditure. He can, being in possession of the latest available figures as regards the progress of expenditure, examine the budget figures with reference to the corresponding figures of the previous and the current years, and point out, where necessary, the errors of facts. The Administrative Department of the Government examines the estimates from the point of view of the department as a whole, and proposes reductions or additions as the case may be. The reductions are communicated to the Accountant-General, and additions to the Finance Department. The Accountant-General forwards his copy of the departmental estimates with his remarks to the Finance Department. The Finance Department goes through these estimates with reference to the explanations of the estimating officers, the remarks of the Accountant-General, and the decisions of the Administrative Department. The procedure outlined in this paragraph is observed in case of the expenditure, which has already been sanctioned and provided for in the estimates of the current year. The Finance Department approves of the figures, which it accepts for insertion in the final estimates, and communicates them to the Administrative Department concerned.

The estimates of the new expenditure are forwarded by the controlling officers to the heads of the departments,

and by them to the Administrative Departments. These do not pass through the Accountant-General. The proposals for new expenditure are, from time to time, submitted to the heads of the department, who communicate them to the Administrative Departments, and the latter send them to the Finance Department for its scrutiny. Their financial effects are then analysed, and the approval or disapproval of the Finance Department communicated to the Administrative Department. The proposals approved of by the Finance Department are submitted to the Government of India for their consideration. The proposals disapproved of by the Finance Department may either be withdrawn by the Administrative Department, or the member-in-charge may submit them to the collective decision of the Government of India. The Finance Member has, in such cases, the opportunity of pressing his objection in the deliberations of the Executive Council. The proposals approved of by the Government of India are either finally sanctioned by them or forwarded to the Secretary of State in Council, in those cases in which his sanction is necessary. The sanctioned proposals are then sent back to the officers from whom they originated who at the time of the preparation of the estimates prepare a list of the proposals of the new expenditure, which is submitted to the Finance Department through the Administrative Department concerned. The latter examines them with reference to the sanctions already accorded, and in light of the new facts which might have later come to light. Some comparatively unimportant items can be included in the schedule of the new expenditure for the first time, and have to be examined *de novo*. After the approval of these proposals by the Finance Department and the sanction by the Government, the Administrative Department prepares an explanatory memorandum on them. This memorandum and the proposals are submitted to the Finance Committee in case of those items for which the vote of the Legislature is necessary.

The Finance Committee is a committee of the Legisla-

ture.[1] It has been constituted with a view to give the Legislature an opportunity of having the estimates thoroughly examined through a committee of its own. The estimates are very intricate and full of wide and varied details. "They," to use the words of Sir Malcolm Hailey, "vary from the field establishment of the geological department to the traffic staff of the State railways," and require, if they have to be intelligently understood, special and technical knowledge, and infinite capacity for taking pains. The only way in which the Legislature can really have a voice in determining the details of the estimates is to have them carefully examined by a committee composed of men, who have made the special study of the financial questions. The Finance Committee can question the propriety of the expenditure, call for explanations, and suggest economies. It can study the proposals in detail and understand their bearing on the financial policy of the Government. The Committee is an advisory body, and its conclusions can, if the Government cannot see its way to accept them, be set aside by it, and the proposals in question submitted to the Legislature on its own responsibility. The Committee only considers proposals pertaining to items, which are submitted to the vote of the Legislature;[2] but in spite of its limited

[1] Functions of the Finance Committee of the Legislative Assembly are:

(1) To scrutinize fresh charges before they are incorporated in the Budget.

(2) To scrutinize the demands for supplementary votes before they are put to the Assembly.

(3) To scrutinize the details of various estimates which are placed before the Assembly.

The Committee is composed of ten elected members to which is added one on nomination by the Governor-General, and the latter is the Chairman of the Committee.

[2] The Finance Member, we are told in the Appropriation Report, Central Revenues for 1922–3, has decided ordinarily to refer to the Committee any new proposals for non-voted civil expenditure with the object of obtaining its advice thereon. As the most important non-voted item is military expenditure, the statement in the text that Finance Committee is concerned mainly with the examination of fresh charges pertaining to votable items is substantially correct.

scope, it can do good work. The members of the committee, on the basis of their knowledge which they acquire as members, can criticize the Government policy in the open house when the Government wants to place a proposal before the Legislature, in spite of its disapproval by the Finance Committee. It is more likely than not that the Government will not go to the Legislature when a proposal has been turned down by the Finance Committee.

Military Estimates.—The principles governing the preparation of the military estimates are the same as apply to the civil estimates but, on account of the peculiarities of military finance, the Army Head-quarters and the Military Finance Branch have a more direct share in the preparation of the military estimates. For the purpose of military administration, India is divided into four divisions, each of which is known as a Command, which comprises a number of sub-divisions named the districts. In each district there is a Military Accounts Officer, who works under the supervision of a Senior Accounts Officer whose office is located at head-quarters of the Command. The estimates are prepared by the administrative officers, and forwarded to the accounts officers, who examines them with reference to figure available in his office, the authorized rates of pay, scales of rations, and clothing and other items which regulate the expenditure on fighting and other auxiliary services. The accounts officers consolidate the estimates, and forwards one copy to the Military Accountant-General, and the other to the chief administrative officers of the Command. The latter examine the estimates, taking into account the observations of the accounts officers, and forwards them with their own remarks to the Military Accountant-General, who compiles the estimates for the whole country. These estimates include only the established charges. Any proposals for fresh expenditure are submitted separately for the sanction of the higher authorities. The preliminary estimates reach the Head-quarters in October and are examined by the Staff of the Commander-in-Chief and the Financial Adviser Military Finance. The estimates

have to be accepted by the administrative officers before they are submitted to the Financial Adviser. The examination of the estimates of established charges does not entail much labour as they are prepared according to the authorized scales, and are examined by the accounts officers before they reach the Army Head-quarters. The proposals for capital expenditure and the expenditure on new measures are submitted by the staff officers for the orders of the Commander-in-Chief. The important proposals have to be taken up individually, thoroughly discussed, and the necessary sanction of the Government of India or the Secretary of State obtained before the preparation of the annual estimates. The Financial Adviser prepares a consolidated compilation of the estimates, submits it to the Commander-in-Chief for his approval, and then places it before the Finance Member. These estimates have to be modified later if the Government of India, after taking stock of the whole situation, cannot spare the necessary funds for meeting all the requirements of military expenditure in the ensuing year.

From the point of view of the tax-payer it is of interest to know the way the proposals for new expenditure on military services are initiated, for we can then assign responsibility for the increase of military expenditure, which is such a striking feature of the military finance in India. The local officers can submit their proposals for fresh expenditure through their accounts officers to the Army Head-quarters, and some of the new measures are introduced in this way. But they are, comparatively speaking, insignificant, and do not contribute materially to the growth of military expenditure. The most important proposals of new expenditure are originated either at the Head-quarters in India or at the War Office in England. The questions of the strength of the fighting forces, the proportion of the British and Indian troops, the rates of pay and allowances, the scales of equipment, accommodation, clothing, and rations, and the apportionment of charges between India and England, are matters with

which the local officers have got nothing to do. The military expenditure, and the rate of its growth, depends upon these matters, and all of them are either settled by the military authorities in India with the sanction of the Secretary of State, or by the War Office in England, whose decisions have to be accepted by the authorities in India, even when they do not approve of them. The financial powers of the subordinate military authorities are limited. They exercise a certain degree of discretion in the purchase of supplies, but otherwise the scale of expenditure is laid down for them, and they have merely to issue money according to it. The estimates of expenditure prepared by the local officers provide for the fixed charges and the fluctuating charges of a routine character. The pressure for increase of expenditure comes from above. The re-organization of the army, the institution of the Military Finance Branch, and introduction of the internal control of the Finance Department on the conduct of military Finance have all failed to exercise any real check on the growth of military expenditure. No amount of changes in the financial machinery can improve matters, so long as the constitutional position with regard to the supreme control remains what it is. The conclusion is in accordance with the generally accepted belief that in matters of military expenditure the need for imposing some sort of popular control is the most imperative. The refinements of financial procedure can be of no avail.

Railway Estimates.—The estimates of the railways are different from the civil and military estimates, as they are both a spending and an earning department; and on account of the magnitude of their operations and liability to respond to the agricultural prospects and trade conditions, they affect the finances of the country in a far-reaching manner. Most of the important railways belong to the State, some of them are worked by the State agency, and others by the companies, and a few are both owned and worked by the companies. It is the State Railways, which have intimate connection with the Government

finances, and whose financial organization has to fit into the framework of the financial system. The methods of preparing estimates of the ordinary expenditure are the same as those which are adopted in other branches of public administration. The primary estimates are prepared by the local working units, submitted to the superior officers who forward them to the railways accounts officers, are examined by the latter with reference to the figures of the past years and the orders of the higher authorities, looked into by the agent of the railway concerned from the administrative and technical points of view, and are then transmitted to the Railway Board through the Accountant-General Railways who, besides being the highest authority in matters of railway audit and accounts, is the officer responsible for the compilation of the railway budget. The rule that no new charge can be inserted in the estimates without the previous sanction of the competent authority is also operative in railway finance, with this difference, that the Railway Board, as the chief controlling authority, enjoys much wider powers for sanctioning new expenditure than the heads of other departments. The Railway Board examines them with the help of the Accountant-General, and submits them to the Finance Department through the Member-in-charge of Railways. The Finance Department does not go through them very critically and confines its examinations to the variations, if any, from the figures of the past years, or any departure from the existing policy. The estimates are then returned to the Accountant-General, Railways.

The estimates of receipts from traffic and other heads are also prepared by the railway administrations, submitted to the Railway Board, which forwards them to the Finance Department. The interest of the Finance Department is greater in the estimates of receipts on account of their bearing on the financial situation of the whole country; it examines them with great care and has been known to make alterations, which have been material enough to give offence to the estimating authorities. But, as the

Acworth Committee[1] pointed out, the officers of the Finance Department, with their long experience, their access to past records, statistics, and information obtained from many quarters and in many ways are in a better position to arrive at a correct forecast of the receipts of the railways than any railway agent.[2] Mr. Cook,[3] in his evidence before the same committee, showed how the modifications by the Finance Department were made as a matter of better estimating and gave instances in which the figures adopted by it were nearer the mark than those of the Railway Board. From the estimated receipts are deducted the estimated working expenses, payment on account of interest, etc., the amount which they expect to spend from the revenues on improvements and renewals, and thereby form an estimate of the probable contribution of the railways to the income of the Central Government or, as has been the case for some years, make a forecast of the deteriorating effect of railway finance on the general finance of the country on account of the inability of the railways even to pay their own way.

The railways are a commercial undertaking, and have to make provision not only for recurring expenses, but also for capital expenditure. The capital expenditure is incurred for special renewals and improvements, as disting-

[1] This Committee was appointed in 1920 by the Secretary of State of India to enquire into the administration and working of the Indian Railways.

The proposal for the separation of Railway from General Finance, which has now been accepted by the Indian Legislature, one of the most important recommendations made by the Committee.

[2] *Vide* Article 23, Acworth Committee Report.

[3] Mr. Cook, the Secretary of the Finance Department, quoted the following figures to show how the Finance Department was more accurate in estimating than the Railway Board.

(In crores).

	Railway Board Estimates.	Finance Department Estimates.	Actuals.
1916–17	55	56⅓	62¾
1917–18	60	62¾	68⅜
1918–19	72	70½	76¼
1919–20	72	80	79
1920–21	81½	84	82

uished from day to day repairs, which are charged to revenues, extension of the existing railways, and opening of the new ones, and is met only out of the borrowed funds, and partly out of the annual revenues of the railways. The interest on these funds is a charge on the railway receipts, though, when the railways cannot even earn their interest charges, the liability has to be met out of the general revenues of the country. The estimates of such expenditure are, also, framed by the agents of the railways, and it is the duty of the Accounts Officer to see that all charges included therein can legitimately be met out of the funds to be provided for the purpose. The Railway Board is to examine them to ensure that the proposed projects are of remunerative character, and may reasonably be expected to earn their own keep after some time, or, in other words, they are "productive"[1] in the sense in which the word is used in the terminology of the Indian Finance Department. The Finance Department in going through these estimates depends upon the assistance of the Chief Commissioner of Railways, who is solely responsible for advising the Government of India in matters of railway policy; and before according its approval to the estimates of capital expenditure, the Finance Department makes a reference to the Secretary of State for India, whose concurrence is essential before such proposals can be finally adopted. The manner in which the funds were provided for capital expenditure till 1923 was strongly criticized by the Acworth Committee, and unsatisfactory condition of railways attributed to what they called the

[1] In order that an undertaking may be classed as productive the following conditions have to be fulfilled:

(1) There must be a good reason to believe that revenue derived from it, in case of railways, within five years, and in case of irrigation projects, within ten years, of its completion repay the annual interest on the capital invested with all arrears of simple interest up to that date and also the capitalized value of land revenue and of leave allowances and pensions.

(2) It must be susceptible of having a clear capital and revenue account of its own.

(3) Its classification as productive public work must be approved by the Secretary of State in Council.

paralysing system of hand-to-mouth finance. The amount of money which was made available for the purpose depended upon the financial exigencies of the year, and many important schemes, with possibilities, could not be executed and, in certain cases, even left half-finished for want of funds. They, therefore, wanted to make the railways immune from sharing the vicissitudes of general finance by emancipating them from the control of the Finance Department, and adopting a guaranteed programme of capital expenditure. The question of separating the railway finance from the general finance is still under consideration,[1] but the other proposal has been given effect to by fixing the capital expenditure at 150 crores as the programme for five years, which is to be strictly adhered to, unless war or some other contingency makes its curtailment inevitable. A guaranteed scheme of finance having been adopted, the railway authorities can work with the definite programme, and lay it out with an assurance that the supplies will not be cut off before it has been fully completed. The estimates of capital expenditure and the estimates of receipts and ordinary expenditure are compiled by the Accountant-General, Railways.

The other commercial department whose estimates are included in the estimates of the Central Government is the Posts and Telegraph Department. The Posts and Telegraph estimates are practically prepared, examined, and approved in the same way in which the railway estimates are dealt with, the difference being that the amount provided for capital expenditure is fixed every year, and is determined by the financial exigencies of a particular year. The amount is, on that account, liable to vary from year to year. These estimates are compiled by the Accountant-General, Posts and Telegraphs.

Ways and Means Estimates.—The Finance Department finishes its examination of the Civil and Departmental

[1] Since the above was written the proposal for the separation of the Railway from the General Finance has been accepted by the Legislative Assembly. The question is further discussed in Appendix IX.

estimates by the end of January, and India Office estimates are also received in India about the same time. The Finance Department knows the amounts of estimated revenue and expenditure which has to be incurred in discharge of public debt, which must be repaid in the following year, and other items of receipts and expenditure in England outside the revenue account. It also knows the surplus of the Central Government, the amount which the Provincial Governments will draw from the balances, which they have got on deposit with the Government of India, and whether these balances are going to be increased or decreased, the amount which is to be spent on capital expenditure for Railways, Post and Telegraphs, etc., several other miscellaneous items of outlay and receipts and estimated opening balance for the ensuing year, and is, therefore, in a position, with the assistance of the Controller of Currency to frame the estimates of ways and means finally which, as already stated, show the amount which the Government of India has to pay out under one head or another, or the sums which it has to receive from taxes, other sources of income and loans. These estimates enable the Government of India to make a forecast of the public liabilities of all kinds and the way in which it is going to meet them. Upon the accuracy of these estimates depends the solvency of the Indian Government.

The Finance Department having received all the receipts of revenue and expenditure consolidates them and the budget estimates are then submitted to the Executive Council for their examination. All important matters involving questions of broad policy and departure from existing practice must have received their consideration, when the particular proposals were being scrutinized from administrative and financial standpoints. It is, of course, open to the Administrative Departments of the Government to appeal to the Viceroy's Council against decision of the Finance Department, and get the disputed matter settled by the majority of the Council as a whole. In a good financial system such appeals should be few,

and the occasions on which the considered decisions of the Finance Members are set aside by the whole Council fewer still. The Finance Member of the Government of India, however, is, as already remarked, not in a very strong position in this respect, and can carry things against the spending departments only when he has the support of the Viceroy himself. When the consolidated estimates are submitted to the Council, their consideration is confined to the review of the financial situation as a whole. The estimates are then assembled in the form in which they are presented, and the Budget together with the supporting statements, are made ready for the consideration of the Legislature.

It has already been stated in the introductory chapter that the whole financial organization of India has been built up on the assumption that the Secretary of State in Council is supreme in all financial matters ; but it has been understood that the control of the Secretary of State over the financial policy and programme of the Government of India is of a general character, and only confined to matters of policy and questions, which raise issues of fundamental importance. In the words of a Government of India despatch,[1] "the statutory control (of the Secretary of State) has been understood to be general, except when the Secretary of State has decided that it must be special." In all stages of the preparation of the estimates, the Government of India is in constant communication with the Secretary of State on important financial matters, and all questions of the change in the nature and rates of taxes, of the amounts of the loans and methods of raising them, all proposals of expenditure for which no precedent exists or those which, according to the decision of the Secretary of State, require his previous sanction,[2] are referred to him

[1] *Vide* Introduction to the Government Audit, by Sir F. Gauntlet. Page 25.

[2] The cases in which the previous sanction of the Secretary of State in Council is necessary are detailed in the rules relating to the expenditure of the Government of India framed by the Secretary of State.—*Vide* Appendix III.

before they are submitted to the Legislature for its consideration; and this is true of both kinds of expenditure—votable and non-votable. When it is remembered that the Legislature does not possess any financial initiative (a point to be explained at length a little later) it will be realized that no important proposal of expenditure, however necessary or desirable, can be considered by the Legislature unless the Secretary of State has given his consent to it. These estimates are not examined by the India Office, but no important proposal can be embodied in them without the approval of the Secretary of State in Council.

Provincial Estimates.—The Rule 37(g) of the Devolution Rules lays upon the Finance Departments of the provinces the duty of preparing the statements of estimated revenue and expenditure, and gives them power to obtain from the departments the materials on which to base their estimates. Under the provision of this rule the Finance Department of each province has issued instructions to the estimating officers for the preparation of the budget estimates. Though there is no absolute uniformity of practice and procedure in this respect, the methods adopted in the different provinces have sufficient similarity to admit of their being described in general terms.

The estimates of revenue, as in the case of the Central estimates, are prepared by the collecting officers on the basis of the actual figures of the previous years, and the anticipated income of the current year. The reasons which have led the collecting officers to adopt the figures proposed by them have to be clearly explained, and any circumstances that, in their view, make variations from the figures of the previous years likely have to be specially mentioned. These figures are carefully examined by the Accountant-General, and the Finance Department, and embodied in the financial statements.

The estimates of provincial expenditure, like those of the Central, are prepared by the various departments, which actually spend the money. The Finance Department sends prescribed forms to the estimating officers in

the months of July or August. The heads of the departments get the subsidiary estimates from the branch departments, but the responsibility for justifying these estimates rests with the officers in charge of the departments. The preparation of the estimates of ordinary expenditure is, for the reasons given already, not a very difficult matter. The estimating officers prepare the forecast of the standing charges which have received official sanction, and for which money has been granted in the budget of the current year. The strength of the sanctioned establishment, the rates of pay, the average expenditure on account of travelling allowances and contingencies being known, the work of the preparation of estimates is a mechanical affair. The subordinate officers submit their estimates to their administrative heads, who forward them to the Accountant-General with their own observations thereon. He examines them with reference to audit registers, sanctions, and any other information that may be available in his office and communicates to the officers concerned any formal changes that he may consider necessary to make. The examination of these estimates by the Accountant-General is generally completed by the second week of September, after which they are sent to the Finance Department. The Finance Department is not concerned with the detailed scrutiny of these estimates and takes for granted that all the charges included therein have received official sanction and been provided for in the estimates.

The estimates of new expenditure have, for obvious reasons, to be prepared with much greater care. The proposals of new expenditure are initiated long before the estimates are prepared, by the heads of the departments, and are to be submitted to the administrative departments of the Provincial Government for its sanction, and generally are not included in the schedule of new expenditure unless this sanction has been obtained. In case these proposals entail expenditure, which require the sanction of the Secretary of State in Council, it is the duty of the Administrative Department to obtain this sanction. The schedule

of new expenditure is sent to the Secretary of the Administrative Department concerned. After its scrutiny by the Administrative Department, it is sent to the Finance Department and is very carefully examined by the latter. According to Rule 37(g) iii of the Devolution Rules, it is the duty of the Finance Department to examine and advise on all schemes of new expenditure for which it is proposed to make provision in the estimates. The function of the Finance Department of the Provincial Government is to act as the organ of financial administration on behalf of the Government as a whole, and harmonize the several demands and conflicting claims. The administrative services are competitors among themselves for the allotment of available funds. It is natural that each one of them should try to secure as much as it thinks it can profitably spend for the prosecution of their particular undertakings. It is the duty of the Finance Department to keep these demands within bounds, adjust the different claims and see that no department is favoured at the expense of the others. The Finance Department, after it has completed its scrutiny of these estimates submits them to the Finance Committee[1] of the Provincial Legislature which, as in the case of the Central estimates, examines them on behalf of the latter. After the consideration of the items of new expenditure by the Finance Committee the Finance Department incorporates these charges in the consolidated estimates.

[1] The functions of the Provincial Finance Committees are determined by the Provincial Governments. The functions of the Punjab Finance Committee may be taken as typical:

(1) To advise the Government on all proposals for new expenditure which require the sanction of the Legislative Council, before they are submitted to the Council.

(2) To advise on such proposals for re-appropriation within the competence of the Finance Department as the Finance Department refers to it.

(3) To exercise such powers of re-appropriation within the competence of the Finance Department as the Council may authorize it to exercise.

(4) To advise the Government on such matters connected with the finance as Government may refer to it.

The Finance Committee in the Punjab is composed of thirteen members, of whom eight are elected, three are nominated and the Finance Membe who is ex-officio member and Chairman of the Committee.

The position of the Finance Department in the Reformed Constitution of India is of great importance in connection with the estimates, and a satisfactory discharge of its duties is a matter of considerable difficulty. The department is, as is well known, a Reserved department. All proposals for new expenditure, whether pertaining to the Reserved or the Transferred half of the Provincial Government, have to be submitted to it for its consideration and advice, and no scheme of new expenditure can be provided in the estimates which has not been so examined. The possibility of this power being exercised in a manner as to detract from the authority of the ministers in the management of their portfolios was considered by the Government of India in one of their important despatches on Constitutional Reforms and dismissed as more or less imaginary. It was pointed out that the Finance Department would not have overriding power in the formulation of the financial policies. It would not dictate or veto the decision. Its main functions would be to watch and advise. But in spite of all that the Finance Member might have to say regarding the necessity or expediency of a particular policy from the financial standpoint, in the last resort administrative considerations must prevail. The ministers as well as the executive councillors would have the power of overruling the objections of the Finance Department, and take the full responsibility for so doing. It may be admitted that in the transitional stage of the political development of the provinces, a unified Finance Department can render very useful service, and will, even when the full responsible government has been attained, be a necessity in the interest of the sound administration of provincial finances. The financial "still small voice" which will urge the considerations of vital importance, protect the tax-payers from being saddled with unnecessary or unduly heavy expenditure, and give a unity and cohesion to the working of the whole financial apparatus, will be needed when the provinces are completely autonomous, and external control has been entirely withdrawn.

"Finance," as the Government of India put in their despatch of the 5th March, 1919, "apart from being the fuel to the whole administrative machine, is a symptom and gauge of the quality of its government," and it will be necessary at all times to have an efficient department to act as the custodian of the financial interests of the provinces. But it must be also be admitted that the relation of the Provincial Finance Department with the transferred departments is one of those anomolies, which have to be tolerated because, to use the words of the authors of the joint report, "they bear on their faces their transitional character." The exercise of the power which the Finance Department possesses must in practice be hedged round with conventions that make its abuse in thwarting the popular half of the Provincial Government in the execution of its plans impossible. It is not possible to say whether during the period that the Reforms have been at work, such traditions have been growing, but there can be no difference of opinion that it is highly desirable that they should, otherwise the smooth working of the complicated arrangement, which depends upon the co-operation of the persons with divergent points of view is almost out of question.[1]

The estimating officers in the provinces are concerned with the preparation of the forecast of expenditure in India. The estimates of the charges to be incurred in England on behalf of the Provincial Governments are prepared by the Secretary of State and the High Commissioner for India. The expenditure of the Secretary of State consists of small sundry items for which he prepares his own estimates. The expenditure of the High Commissioner represents the cost of stores purchased or payable in England requisitioned by the departments of the

[1] Since the above was written the Ministers of the different provinces have in their evidence before the Reforms Enquiry Committee thrown interesting light on the inner working of the Provincial Governments from which it appears the Finance Departments of the provinces have not been able to inspire confidence in the minds of the popular half of the Provincial Governments regarding their impartiality or fair-mindedness. The situation is obviously unsatisfactory, but it is difficult to suggest measures for improving it.

Provincial Governments, leave and deputation allowances, pensionary charges, and any other class of expenditure. The budget estimates of stores are prepared by the High Commissioner on the basis of the forecast forwarded by the Provincial Government. The departments of the Provincial Governments submit to the Finance Department an estimate of their requirements with a forecast of the value in respect of stores, which under the rules have to be purchased in England. These estimates consist of two parts—one of the ordinary expenditure, and the other of new expenditure—which are consolidated by the Finance Department, and forwarded to the High Commissioner. The Finance Department does not examine them at this stage. The High Commissioner modifies them with reference to more up-to-date information at his disposal as regards prices, etc., and sends them back to the Finance Department, which subjects them to a careful scrutiny, submits the items of the new expenditure to the Finance Committee, and then includes them in the consolidated estimates. The estimates of expenditure on leave allowances and other miscellaneous items are also prepared by the departments concerned, sent to the Finance Department, and are incorporated in the estimates after they have been sent to and received back from the High Commissioner. The estimates of the pensionary charges are prepared by the High Commissioner, and sent to the Finance Department for inclusion in the provincial estimates. The High Commissioner is not under the administrative control of the Provincial Governments, but the estimates prepared by him have to be carefully examined by the Finance Department as the estimates of the other expenditure.

The departmental estimates having been examined by the Finance Department and Finance Committee, and the estimates of expenditure in England included therein, are now ready for the consideration of the Provincial Government as a whole. This is the most difficult stage in the preparation of the provincial estimates. The difficulty

was fully appreciated by the various authorities, when the Reforms were on the anvil, and the crucial character of the question viewed with great misgivings. A number of expedients were considered for avoiding a deadlock between the two halves of the Provincial Government, in the matter of allocation of revenues, and set aside on account of their inherent defects.[1] The scheme of what the Government of India called the pooling of revenues was finally adopted and put into operation.[2] The two halves of the Government consider the estimates together, and try to come to an agreement with regard to the distribu-

[1] The Government of India was in favour of giving to each half of the Government separate purse of its own in order that there may be no occasion for the financial arrangement breaking down on account of the failure of the two halves to come to an agreement regarding the apportionment of the provincial revenues. This suggestion was not accepted by the Joint Select Committee of the Parliament.

[2] Sir Frederick Gauntlet explained the reasons which led to the introduction of joint purse in the following words in his evidence before the Reforms Enquiry Committee:

Q.—Are you in a position to tell us—I do not suggest that it is within your knowledge—can you tell us what considerations finally led to the decision to have a joint purse rather than a complete separation of revenues on the reserved and the transferred side?

A.—The original idea undoubtedly was for separate purses; and when it was considered in detail, the difficulties that were found were so great that it was thought preferable to have a joint purse. One or two points I can still remember as arising in the course of those discussions. First of all, how are you going to divide your purse? What method would you adopt? You might easily take a fixed proportion, say 50 and 50, that is to say 50 per cent shall be for the reserved side and 50 per cent shall be for the transferred side. It was recognized that there would be much greater need for development on the transferred than on the reserved side. So that if you start with 50 and 50, and keep that distribution, with the growing revenues, you will very soon find reserved side building up huge balances which it does not want, while the transferred side very quickly spends all that it has got and wants to spend more. If you have two branches of work, one developing much more rapidly than the other, a fixed division of the joint purse is not the proper method of providing funds for those two separate classes. Then take another point. Assume that you start with a division, and as I have indicated, the transferred side, the Ministers find that they want more money than has been given to them under the distribution. The need for further taxation then arises, so that you have to divide your field of taxation. You want to find out what sources of taxation are recognized as the legitimate field for the Ministers. How are you going to divide your sources of taxation? That was found to be a very great difficulty, and the difficulties were so great that it was eventually decided that simplest thing was to start with a joint purse and only adopt the separate purse if you were driven to it.—*Vide* Appendix VI to the Reforms Enquiry Committee Report, p. 108.

tion of funds. Provision has been made for the distribution of funds when there is an irreconcilable difference of opinion between the two halves of the Government,[1] but the occasion for the exercise of the contemplated device has not so far arisen; and the presumption is that during the short period that the arrangement has been at work, its use has been obviated by the process of reasonable give and take on which the working of the whole constitution depends. But it cannot be denied that the situation has in it the possibility of acute friction. Implicit reliance cannot be placed on the reasonableness of the parties concerned, and the allocation of revenues by the Governor or authority

[1] *Vide* Rules 32, 33, and 34 of the Devolution Rules, Appendix II:

In this connection it is worth while to give an extract from the Report of the Joint Select Committee on the Government of India Bill. It says, "The Committee has given much attention to the difficult question of the principles on which the provincial revenues and balances should be distributed between the two sides of the Provincial Governments. They are confident that the problem can be readily solved by the simple process of commonsense and reasonable give and take, but they are aware that the question might in certain circumstances become the cause of much friction in the Provincial Government, and they are of opinion that the rules governing the allocation of revenues should be framed so as to make the existence of friction impossible. They advise that if the Governor in the course of preparing its first or any subsequent Budget finds that there is likely to be a serious or protracted difference of opinion between the Executive Council and the Ministers on the subject, he should be empowered at once to make the allocation of revenue and balances between the reserved and the transferred subjects which should continue for at least the whole life of the Legislative Council. The Committee does not endorse the suggestion that certain sources of revenue should be allocated to the reserved and certain sources to the transferred subjects, but they recommend that the Governor should allocate a definite proportion of its revenue, say by illustration two-thirds to the reserved and one-third to the transferred subjects, and similarly a proportion though not necessarily the same fraction of the balances. If the Governor desires assistance in making this allocation, he should be allowed at his discretion to refer the question to be decided by such authority as the Governor-General might appoint.

The Committee desire that the relation of the two sides of the Government in this matter, as in others, should be of such mutual sympathy that each will be able to assist and influence for the common good the work of the other, but not to exercise control over it. The budget should not be capable of being used as a means for enabling the minister or the majority of the Legislative Council to direct the policy of the reserved subject, but on the other hand the executive council should be helpful to the ministers in their desire to develop the subjects entrusted to their care. On the Governor personally will devolve the task of holding the balance between the legitimate needs both sets of his advisers.

appointed by the Governor-General will not, when the occasion arises for the use of this power, solve the difficulty. The arrangement will need revision as soon as the question of further constitutional advance becomes a subject of active negotiations. As it is both the executive councillors and the ministers come to an understanding as to how the revenues are to be shared, and what taxes are to be imposed, if the income from the existing taxes is held inadequate for meeting the expenditure of the ensuing year.[1] The matters pertaining to the raising of loans[2] are also considered by the Provincial Government as a whole. It need not be added that in the deliberations of the Provincial Government the opinion of the Finance Member is given due weight, and in all questions relating to the increase of the revenues of the Province it is generally decisive.

Before the Reforms the budgets of the Provincial Governments were submitted to the Government of India before they were placed before the Provincial Councils. It was complained that the Government of India modified the estimates of the Provincial Governments, and made many meticulous alterations. With the assignment of distinct resources and more final powers to the Provincial Governments, the Government of India does not exercise any detailed control over the financial proceedings of the provinces. The budget estimates are finally settled by the Provincial Government, and the Governments require information relating to the provincial estimates regarding the withdrawals of their balances or any addition thereto, and the amount of assistance, if any, which the Provincial Government may require from the Central Government in the shape of loans and the amount of repayment of such

[1] As a rule all proposals of taxation or borrowing on the security of the provincial revenues are considered at the joint sitting of the two halves of the Government, but each half has the right to originate its own proposals and arrive at a decision with regard to them separately.—*Vide* Rule 30, of the Devolution Rules.

[2] The objects for and the conditions under which the loans can be raised by the Provincial Governments have been laid down in the Local Government Borrowing Rules.—*Vide* Appendix II.

loans.[1] The information is necessary to enable the Government of India to frame their ways and means estimates. The Government of India do not now retain any hold over the balances of the Provincial Governments. As explained in a later chapter, all Government payments are made by, and the receipts paid into the treasuries, sub-treasuries, the local head offices of the Imperial Bank and its branches. The Government of India are responsible for meeting all public obligations, its own, and that of the Provincial Governments, and have, therefore, to make adequate provision for the anticipated liabilities of the ensuing year. As the Government of India has to maintain a common exchequer for all public receipts and disbursements, it cannot assume an attitude of complete indifference towards the provincial estimates. If and when the Provincial Governments have their own treasuries or independent banking accounts, the Government of India can exempt the Provincial Governments from the requirement of furnishing any information relating to the provincial estimates. The Government of India will even then have to devise measures[2] for providing against the extreme contingency of any Provincial Government not being able to meet its liabilities but that will require only a certain amount of general supervision. It will not be necessary for the Provincial Government to furnish any information with regard to their annual estimates. The information required by the Central Government is due on the 15th January—just about the time, when the compilation of the Central estimates is completed and the ways and means

[1] The tax which the Provincial Governments can levy or whose rates they can vary without the previous sanction of the Government of India are given in the Scheduled Taxes Rules.—*Vide* Appendix II.

[2] The Government of India, besides the two main points referred to above, also requires information relating to the provincial budgets on the following points:

(1) The opening and closing estimates for the next year of the Famine Insurance Fund.

(2) The extent to which it is proposed to pay off the Provincial Loan Account in the coming year.

For Famine Insurance Fund see Chapter V, and for the Provincial Loan Account see Chapter XII.

forecast is framed. The applications for being allowed to raise loans on the security of the provincial revenues have also to be submitted about this time.[1]

Form of the Estimates.—The general conditions bearing on the form of the estimates have been stated already. The data regarding the revenue estimates of the State can be compiled only according to the sources from which the revenue is derived. But the data of expenditure can be compiled from different standpoints. The estimates of

[1] Mr. J. E. C. Jukes, C.I.E.I.C.S., Officer on Special Duty in the Finance Department thus summarizes the position of the Provincial Government in the matter of the financial autonomy:

"Certain sources of revenue are placed at the disposal of the Local Governments from which to finance the provincial administration. If it is desired to supplement the revenue raised from these sources, recourse may be had either to taxation or to a loan. In the former case no sanction beyond that of the provincial Legislative Council is required if the tax is one of those sheduled by the Scheduled Taxes Rules. If it is not so scheduled, the sanction of the Governor-General in Council is required to the tax. If the Local Government desires to raise a loan, it has two alternatives open to it. It may apply to the Government of India for an advance, which may be given under Devolution Rule 25 on such terms as the Governor-General in Council may prescribe; or if the loan is to be spent on one of the objects specified in the Borrowing Rules, it may ask the sanction of the Governor-General in Council to the flotation of a loan in the open market. All provincial revenues and moneys, from whatever source received, must pass into the public account, of which the Governor-General is the custodian. They may ordinarily be withdrawn by the Local Government on conditions prescribed by the Governor-General in Council, but the latter has the right in case of emergency, to refuse to permit withdrawal. While they remain in the public account, they are entirely at the disposal of the Central Government, which employs them for its own ways and means purposes. As regards expenditure from provincial balances, there are, in case of transferred subjects, very few instances in which the sanction of the Secretary of State in Council is required to expenditure, though one of the instances covers the large requirement of the observance of the fundamental rules. Apart from these instances, the powers of the Local Government are unfettered. In relation to the reserved subjects: the powers enjoyed by the Local Government are considerably smaller. Revenue and expenditure are brought to account by an establishment which is in no way under the control of the Local Government. As regards general control both the Secretary of State and the Governor-General in Council have practically abandoned their powers of superintendence, direction, and control in respect of transferred subject, though they have retained them in relation to the reserved subjects. Finally the grant of financial autonomy conferred by the Act and Statutory Rules is conditioned upon maintenance of Famine Insurance Fund on prescribed lines and, secondly, the institution of a Provincial Finance Department exercizing powers similar to those delegated by the British Parliament to its own Treasury."—*Vide* Appendix V to the Reforms Enquiry Committee Report, pp. 440–41.

the Indian Government are based on the units of organization—that is, the forecast of expenditure is made with reference to each branch of government, department or sub-division of department, which will incur or control it, and not to the object for which the expenditure will be made. The estimates are built out of the system of accounts, which is so devised as to make the development of the data of the financial conditions and the operations of the Government possible. The method of presenting the data is to proceed from the general to the particular. This principle is adhered to in all estimates of Home, Central, or Provincial Governments.

The Home estimates are incorporated in the estimates of the Central Government under appropriate heads. But according to the Act, the Home accounts of the Government of India have to be submitted to the Parliament, which also include the estimates of the current year.[1] Generally speaking there are five columns in the form of the estimates: in the first, the service provided for is described; in the second, the amount to be spent for is specified; in the third, the amount spent for the purpose in the previous year is stated; and the fourth and fifth columns are for showing the increase or decrease respectively, which the comparison of the amounts entered in the second and third columns indicates. The estimates are supported by the details of salaries, establishments, etc., on which they are based. The estimates of expenditure of the High Commissioner for his office, establishment, etc., are also shown in the Home accounts. These are accompanied by an explanatory memorandum of accounts and estimates.

The budget estimates of the Central Government are submitted to the Indian Legislature. The central and basic element of these estimates, of course, is a comprehensive balanced statement of estimated revenue and expenditure for the ensuing fiscal year. But, standing by itself, this statement cannot give the amount of information

[1] As the Indian estimates are presented to the Parliament in May they become the estimates of the current year.

which the Legislature, as the fund-granting authority, requires for appreciating the financial situation. In the statement (I) are included the actual figures of the previous year, the budget estimate and revised estimates of the current year, and the budget estimates of the coming year. The estimates are classified according to broad divisions in which the sources of revenue and the heads of expenditure are grouped. The first column is for revenue or expenditure heads, second for the accounts of the previous year, the third for the budget estimates of the current year, the fourth for the revised estimates relating to the same year, and the fifth for the budget estimates of the following year. In the statement (II) is given the information regarding the receipts and the disbursement of the Central Government outside what is called the revenue account.[1] On the receipt side, besides the estimated surplus, if any, are shown the amount which are to be received by borrowing, through deposits, repayment of loans, the unspent balances of the Provincial Government and similar other transactions. On the disbursements side, are shown deficit, if any, the amount to be spent for railways, irrigation posts and telegraphs, etc., from borrowed funds, amount which is to be paid for discharge of debts, balances withdrawn by the Provincial Governments, and the transactions of the same nature. The arrangement of columns and the purposes for which they are intended are the same in this statement as in the statement (I) and this is true of all other statements which comprise the budget estimates. The statements (I) and (II) being of a general character are followed by statements which give more detailed information. The statement (A) shows the amounts to be received from the different sources of revenue under each head. The statement (B) gives similar information with regard to expenditure to be incurred for the main departments of the Central Government. The statement (C) gives the

[1] The Revenue Account is the account in which the income from taxes and other ordinary sources of revenue and expenditure other than that which is met out of the borrowed funds and similar other receipts is shown.

detailed information regarding receipts and disbursements. In the statements (A), (B), and (C) the figures for the amount to be received and spent in India and England are shown separately. The statement (D) is an abstract of the statements (A), (B), and (C). The statements (I), (II), (A), (B), (C), and (D) comprise the budget proper. But these statements, comprehensive as they are, would not in themselves be adequate for the exercise of effective financial control by the Legislature. The information which they convey has to be supplemented by details which enable the Legislatures to know how the amount entered in them has been made up. These details are set forth in two volumes. The first, which is the most important from the standpoint of the public, is entitled "Detailed Estimates and Demands for Grants." This volume contains detailed estimates in support of the proposals for the grant of funds other than those for railways and posts and telegraphs as well as the estimates for which the sanction of the Legislature is not required, other than military services. The estimated expenditure on railways, posts and telegraphs is shown under certain main heads and the details are given separately on account of the magnitude of the amounts involved and the technical character of the services themselves. A separate proposal is ordinarily made in respect of grant proposed by each department, though the Finance Department has the discretion of including in one demand grant proposed for two or more departments or sub-dividing a proposal for one department into two more parts. Each proposal is called "Demand for Grant." There are sixty-three such demands in the estimates for 1923–24. Each demand[1] first takes the total amount which is required for the service concerned and is followed by detailed estimates of the sub-divisions known as the minor heads, which are again sub-divided into units, which are generally uniform and comprise pay of officers, pay of establishment, travelling allowances,

[1] For list of Demands for Grant and a specimen of a Demand.—*Vide* Appendix III.

other allowances and honoraria, and supplies and services. The sub-heads of minor heads are called the Units of Appropriation. These units of appropriation are further supported by the information regarding the personnel, their rates of pay, and other items of minute details. The distinction between the total amount assigned for a particular service, which when sanctioned is called a grant, and that assigned for minor head is that while the former cannot be exceeded without the specific sanction of the Legislature, or the funds allocated for it diverted to another service, the transfer of sums assigned to the latter to another minor head is permissible under certain conditions. In the form of the demand, as in the statements mentioned above, columns are provided for actuals of the previous year, and budget estimates of the ensuing year : but the last three columns are divided into two parts to differentiate the amounts for which the vote of the Legislature is required, and those which are not submitted for its vote but are inserted in the estimates for its information. The new items of expenditure are printed in thick types and non-voted ones in italics. The new items which have received the approval of the Finance Committee are marked with asterisks. The footnotes furnish a brief explanation of important variation. The estimates for each minor administration like Delhi, Coorg, and Baluchistan are brought together under a separate demand for each area. In the end of this volume the notes of the Finance Secretary explaining the details of the main heads of receipts and expenditure are also included. These notes are generally brief and deal with all the financial operations of the Government of India. The detailed estimates of posts and telegraphs and railways are printed as appendices of the volume of detailed Estimates and Demands for Grants. Appendix A gives the details of estimated expenditure of the posts and telegraphs, both for working expenses and capital outlay. Appendix B contains details of estimates of railway expenditure chargeable to revenue, and the Appendix C those of the estimated capital expendi-

ture on railways. These details are, from the nature of things, different from those of the other Government departments and, with the exception of the working expenses of posts, and telegraphs, are not set forth in the manner described above. The railway estimates do not give information regarding the specific items of expenditure. In the Appendix B the estimates of receipts are classified under three heads: Coaching Traffic, Goods Traffic, and Other Earnings, and the estimates of expenditure under ordinary working expenses, fuel, and programme revenue expenditure, viz., the amount which it is proposed to spend on renewals and repairs. The ordinary working expenses are shown under the sub-heads (a) General Superintendence, (b) Operating Expenses, (c) General Charges, (d) Ordinary Maintenance, (e) Unclassified Expenditure. But the details regarding the personnel, rates of pay, etc., which are given in case of the civil and military estimates are not given except for appointments carrying a salary of rupees one thousand or more. The minute details, if included in this appendix will make it bulky, but will be useful for enabling the members of the Legislature to have a full and detailed information about the railway expenditure. In Appendix C the information is given according to the different schemes for which the capital outlay is required. The details of the estimated expenditure on military services and connected receipts are given in the other volume. The underlying principle according to which the military estimates are classified is the same—to proceed from the general to the particular. They are divided into three sections according to the three main branches—Army, Marine, and Military Works. Army estimates are again divided into three parts: (A) Standing Army, (B) Auxiliary, (C) Territorial Forces and Royal Air Force. Part (A) is divided into seven sections, part (B) into five and part (C) into eight sub-sections, which are further sub-divided according to the constituent units and other organizations on which the expenditure is incurred. The marine and military works estimates are classified on the same basis. The military estimates are given in very

great detail, but the primary units of expenditure are different from those of the civil estimates on account of the character of the services to which they relate. The military expenditure not being subject to the vote of the Legislature, there are no columns in the detailed estimates for voted and non-voted expenditure. These statements, general and detailed, would fall short of giving a really illuminating account of the financial situation if its salient features were not described in the speech which the Finance Member delivers while introducing the budget in the Legislature. This speech constitutes a review of the whole financial situation. It explains the financial events of the current year, presents financial policy and programme of the Government of India for the coming year, and is the announcement of the ways in which it proposes to meet the estimated expenditure, both on revenue and capital account. This speech is the last step in a long series of events, which leads up to the presentation of the estimates to the Legislature, and it is also the most important. It is the culminating point of one stage in the financial proceedings of the Government and starting point of another.

The form of the provincial estimates need not be described at length as there is no material difference between it and that of the central estimates. There are, of course, variations in detail on account of difference in the conditions for which they provide, but the accounts from which these estimates are developed are maintained on the same basis as the central accounts and, therefore, do not leave much room for any important changes. There is one variation, however, which requires special notice. The whole system of provincial administration being divided into two halves, reserved and transferred, this distinction runs through the whole structure of provincial estimates as all items of expenditure either relate to the reserved or transferred half of the Provincial Government. The information about the revenue, expenditure, receipts, and disbursements is presented under broad divisions, and is

supported by more detailed information under the main heads of revenue and expenditure, and by detailed estimates under all heads of revenue and expenditure with special appendices for certain large-spending departments, for example, the Buildings and Roads Branch, Irrigation Branch and the Forest Department. These statements are accompanied by a memorandum in which all variations and figures of revenue and expenditure and new items of expenditure are explained. The detailed information is given according to the broad divisions, minor heads, and the units of appropriation. The estimated expenditure for which the vote of the Legislative Council is needed is set forth in a series of proposals for the grant of money which, as in the case of the central estimates, are called Demands for Grant. There is usually one demand for each department, but the Finance Department can combine the grants required for two or more departments into one demand or split the grant for one department into two or more demands. The full details of expenditure, over which the Legislature does not exercise any control, are also given for its information. In all these statements, abstract or detailed, figures for the previous years, budget and revised estimates of the current year are given for comparison with the budget estimates of the coming year. All proposals for new expenditure are distinctly shown in order to give them due prominence. These budget statements are introduced in the Legislature by the Finance Member, with a speech, the nature and the scope of which is the same as that of the speech which the Finance Member of the Government of India delivers in presenting his budget to the Central Legislature.

Supplementary Estimates.—The budget estimates, being in the nature of a guess of the coming events, are likely to turn short of or beside the mark on account of the unforeseen developments, which have to be subsequently provided for. The Central and Provincial Governments have, in order to get the Legislature to grant funds for the unforeseen and unprovided-for public needs prepare what are known as the Supplementary Estimates. The question

as to whether it is desirable to let the Executive apply for the grant of funds, the demands of which have not been included in the original estimates, is a little complex and will be dealt with in the next chapter. Here it may be stated that the procedures of preparing and the form of these estimates is the same as those of the original estimates.

General Observations.—It will not be amiss to conclude this chapter by offering a few general observations on the preparation and the form of Indian Estimates. The first observation that may be offered is that the estimates, central and provincial, in theory, though not in fact, emanate from the Executive as a whole. That is so in theory as far as the central estimates are concerned, and though duality is the distinctive feature of the provincial administration, and is implicit in the provincial estimates, they should, to the extent to which the Diarchy is not an utter failure, bear on them the impress of "mutual advice and consultation." The integrity of these estimates is considerably impaired on account of the ultimate political control being vested in an authority who has neither the opportunity nor the inclination to consider them in their entirety. But the estimates when they are presented to the Legislature are, in theory at least, the act of the Executive; and though the practice is different from theory, its acceptance is a matter of some importance, as the constitutional progress of the country will narrow the gulf between the two, and ultimately establish the tradition of the solidarity of the executive responsibility. The collective responsibility of the Executive for the financial programme of the year must be a cardinal principle of a good financial system, otherwise it is not possible to impart to the budget estimates the qualities of unity, equilibrium, and comprehensiveness, which are so manifestly desirable. The defect of practice in India is due to causes which will cease to be operative as soon as India can assert her right to political maturity by effective political action, and the theory, which is inherent in the system of financial

administration, will then become a regulative principle of very great importance.

The Executive responsibility of the Budget estimates carries with it the necessity of an organ of financial administration, through which the responsibility thrown on the Executive can be effectively discharged. The Finance Departments in India are expected to perform this important function. They are expected to have the power of direction, supervision, and control over the financial administration and the preparation of the budget estimates. The status and powers of these departments ought to be quite distinct from and superior to the other administrative services. But they are, under the existing circumstances, labouring under great disadvantages. The estimates of the Secretary of State are not subject to the scrutiny of the Central Finance Department. The spending departments of the Government of India—particularly the military—are not amenable to its control to the extent to which it is desirable, if the interests of economy and efficiency are to prevail in financial matters. The Provincial Finance Departments have, in their present form, been brought into existence by the Reforms. They have to provide for expenditure which is not under their control. The financial administration ought to be conducted by them in a manner which, while preventing waste, inefficiency, or undue pampering of a particular service, should not expose them to the charge, well-merited or otherwise, of becoming an instrument of the reactionary elements in administration. They do not enjoy the prestige which comes from the traditions of the past or the existence of vigilant and powerful Legislatures, which in all democratic countries are very helpful allies of the Treasury. A far-sighted view of the matter, however, will enable us to look at these Finance Departments, the central and provincial, from the standpoint of not what they are but what they will become when India becomes a self-governing country and has a completely democratic constitution. The provision in the present constitution that all departmental estimates must

pass through and be approved by the Finance Departments and no new charge be inserted therein which has not been examined and generally speaking sanctioned by them, which must now be a source of annoyance on certain occasions, will have a different significance, and make the democratic control of the national finances a reality. The political progress of the country will make the Finance Departments, what they ought to be even now, the guardians of the people's purse, and "the taskmaster of the servants of the State, charged with the necessary but ungrateful task of requiring from each a fair day's work for a fair day's pay."

But if the Finance Departments are to effectually discharge the duties of financial control, they themselves should have nothing to do with the actual performance of the work of the Government, or in other words they themselves should not be spending departments. The Finance Departments cannot resist the demands of other spending departments if they themselves initiate schemes which involve heavy expense. Their sole function should be to ensure compliance with the regulations formulated by them for the guidance of the spending departments and act towards their estimates, to quote E. Hilton Young, as *advocatus diaboli*—be champion of economy against the champions of spending. E. Hilton Young regrets from this point of view the recent developments which have made the British Chancellor of Exchequer responsible for large headings of expenditure like the Old Age Pensions, and is afraid lest the traditions of the nineteenth century which have made him the watch-dog of economy may, on that account, be not maintained in the twentieth.[1] The old

[1] Willoughby makes the following remarks on the same facts:

To the statement that the Treasury is not a public service department or a spending department one serious exception must be made. For reasons which are not clear the National Insurance system has been placed under the administration of the Treasury. As a result of this policy the Treasury is now responsible for the expenditure of a huge and growing sum of money. This constitutes a serious break of the theory on which the organization and functions of the Treasury rest. The departure has not escaped criticism. It is very pertinently pointed out

traditions cannot be easily weakened but it is difficult to build the new ones. The practice which exists in the Government of India and the provinces of placing the Finance Members in charge of the other portfolios besides that of finance cannot be regarded without misgivings in view of the necessity of making the Finance Departments the custodian of the interests of the taxpayer. They, in order to question the propriety of the schemes of expenditure brought forward by other Administrative Departments should be able to do so with dignity and impartiality which can only be attained if they themselves hold aloof from the administrative work of the Government. The Finance Departments, if they are to pass judgment upon and harmonize several demands of the various departments, should not have claims of their own which they may be suspected of specially favouring at the expense of others. This aspect of the work of Finance Departments has not received any attention, but needs special emphasis on account of its great importance from the standpoint of developing right traditions in the financial administration of India at this stage of her constitutional history.

Those estimates are not examined by the India Office; but on account of the references which have to be made to the Secretary of State under the rules or charges which have to be included in the estimates on account of the adoption of the measures initiated by him, the financial discretion of the administrative authorities in India is considerably circumscribed. In the opinion of the Acworth Committee the relaxation of control exercised by the Secretary of

that whereas the Treasury formerly had the duty of questioning proposals for the expenditure of money brought forward by others, it is now itself an applicant for funds on a large scale. It is thus in the anomalous position where it is its duty to question its own proposals or to let those proposals go without question. Manifestly the Treasury powers to resist demands for funds brought forward by other departments is weakened by the fact that it is itself in the field for increased grants."—*Vide* n., p. 180, of the "British Financial Administration," by F. W. Willoughby and others.

Since the above was written the Reforms Enquiry Committee has recommended that the Finance Members should not ordinarily be placed in charge of any important spending department.—*Vide* para. 110 of the Reforms Enquiry Committee Report.

State in matters of railway finance is overdue. The withdrawal of this control in matters of general finance, though highly desirable, depends upon radical constitutional changes. But the Secretary of State can let certain conventions grow which may leave the authorities here greater freedom in the preparation of the budget estimates. In the interest of sound financial administration, if nothing else, it is necessary that financial control be reduced to the minimum. It is well known that the Secretary of State has during the last three years been interfering oftener in all matters, including financial, than he need or ought to have if the Reform Act had been worked in the manner in which the Joint Committee, in their oft-quoted passage, wanted it to be worked. The matter has wider aspects than financial, but its bearing on the working of the financial system is obvious, and points to the conclusion that the continuance of intervention bythe Secretary of State in financial matters is anomalous and subversive of sound methods of transacting financial business.[1]

[1] Sir Frank Nelson, who cannot be called an impatient idealist, made the following remarks in his speech in the Annual General Meeting of the Bombay Chambers of Commerce: "The present divided control of the Indian Finance, partly in India and partly in Whitehall, cannot be in the best interest of the country. A natural concomitant of the Reforms should be the centralization as soon as may be of the entire control of Indian Finance, Currency, and Exchange in the person of the Finance Member, who in turn must justify these gravely important subjects to the Legislative Assembly."

CHAPTER IV

ESTIMATES IN THE LEGISLATURES

THE word " budget " has been frequently used in the preceding chapter. In view of its importance it is desirable to attach precise meaning to it. In spite of the fact that the word is in common use there is no general agreement regarding its exact significance. Henry Higgs defines it as an estimated balance sheet of revenue and expenditure of the financial year.[1] In the Government of India Act, the Indian Budget has been referred to as the estimated revenue and expenditure of the Governor-General in Council.[2] An American writer describes it as the whole scheme of national finance and takes it to mean as the arrangement according to which money is asked for by the Government, voted by the Legislature, spent by the Executive, and controlled by an agency independent of the Executive who submit a report regarding the expenditure to the fund-granting authority. It may be stated with asurance that the budget is not merely an estimate of revenue and expenditure. That is not the sense in which it is commonly used. Budget, if it is merely an estimate, would not be, as Willoughby puts it, " the master problem of our public administration."[3] The rôle which this word has played in the constitutional history of democratic countries suggests a great deal more. An estimate can be prepared by an agent of an enlightened despot for the information of the latter in order that there may be some method about the manner in which money is raised and spent in his domain. That is the object with which the estimates are still prepared in some of our leading Native States, and though

[1] *Vide* Higg's " Financial System of the United Kingdom," p. 37.
[2] *Vide* the Government of India Act, Section 67.
[3] *Vide* " Problem of a National Budget," by H. F. Willoughby.

these estimates are called the budgets they can bear that name only by courtesy. On the other hand, if the budget is given very wide significance and made identical with the whole range of financial operations beginning with the preparation of estimates and ending with the audit of accounts, it will result in confusion of thought and practice. It is customary to speak of preparing the budget, voting the budget, executing the budget, but it is a very loose use of the word. The budget is essentially an instrument of popular government by which the responsibility of the Executive to the Legislature is enforced. It is a document of information with which the Executive comes before the Legislature, gives an account of its stewardship during the expiring year, and lays before it its plans for the coming one. It is, to quote Willoughby again, "at once a report, an estimate, and a proposal." It forms the basis of the financial legislation of the coming year. The contents of the budget are determined by the supreme need of placing before the Legislature the full information about the financial events of the past year, giving it an opportunity of bringing the public administration of the year under review, and on the basis of this information approving or disapproving the programme of the year to come. A word, which originally is said to have meant only a leather bag, has, on account of the historical evolution, come to have a meaning all its own. It is an integral part of the system by which the general will of the nation impresses itself on the conduct of the national affairs.

The "budget," in this sense of the word, has not found a place in the financial system of India in the past, and inasmuch as the popular control of the national finances is incomplete under the Reforms, an effective budget cannot be said to exist even now. The estimates have been prepared in India, and presented to the Legislatures, such as they were, since 1861. But they were neither discussed nor voted upon till 1892. The Act of 1892 gave to the members the right to discuss the estimates, but they could not move resolutions or divide the councils. The Minto-

Morley Reforms empowered the councils to discuss the estimates before they were finally settled, to propose resolutions, and to divide themselves on the issues raised in connection therewith. The Joint Report has summarized the position admirably by saying, "Power remained with the Government, and the councils were left with no functions other than criticism," and "criticism," in the words of Mr. Gokhale, "may be effective as a check, but is not control." The estimates have been called budgets all these years. The methods of preparing them, and the procedure of presenting them to the Legislature were, as far as possible, borrowed from the financial system of the United Kingdom. But the essential feature of the budget system, viz., the supremacy of the Legislature, being absent, the estimates were only budgets in name. The Act of 1919 has given wider financial powers to the Indian Legislatures. These powers are not illusory. The members of the Legislature can make their presence felt in more ways than one. But the most important principle has still to be established. The British financial system fulfils, as is well known, two functions—administrative and constitutional. The Indian system fulfills the former function fairly well, but the latter is exercised under restraints which the present political system makes inevitable. The constitutional importance of reducing the number and scope of these restraints is generally admitted, but their existence, as a vital factor in the Indian financial organization, makes it necessary for us to use the word budget with reservations, which are inherent in the existing state of things. The word, having come into vogue on account of our contact with the country, whose constitutional history, has given it the dignity and the importance, which it possesses, may still be used, but the essential difference[1] between what it means here, and all that it

[1] The difference between the budget in India and the budget in the democratic countries was well expressed by the signatories of the Minority Report of the Welby Commission when they said: "For them (the Indian Executive) the budget is not a binding document. It is a voluntary expression of anticipated expenditure."—*Vide* Welby Commission Report, Vol. IV, p. 157.

means in the democratic countries has to be borne in mind, and should not be obscured by the use of the same word. The difference will persist as long as the determination of the Indian policy is in the hands of an authority not amenable to popular control.

The financial control of the Executive by the Legislature in a self-governing country carries with it the right to consent to the number and nature of taxes, the raising of public loans, and grant of money for expenditure, specifying the amount and the purpose of expenditure and the period for which it is granted. A few items which, for certain reasons, cannot be allowed to vary from year to year, may be made a permanent charge on the revenues of the country, and exempted from the annual vote of the Legislature, but the bulk of expenditure requires its sanction every year, and the public opinion does not tolerate any departure from this constitutional practice. All taxes, or at least some, the income from which is sufficiently large to make it impossible for the Executive to carry on the administration without them, remain operative only for a year, and have to be renewed annually with the consent of Legislature. Any changes in the rates of taxes, or the imposition of a new tax, or remission of an old one, cannot be brought about without the express sanction of the Legislature. The Executive cannot float any loans without obtaining the permission of the Legislature and, of course, before the sanction is granted, the purpose, the rate of interest, and the conditions of the loans have to be scrutinized and approved. These rights give to the Legislature what is commonly called the power of the purse, which implies the right to determine the sources of income and the amounts and objects of expenditure. The Indian Legislatures will, when they have served their apprenticeship, have all these powers, if they are to become supreme in all matters. The powers which they possess in the present constitution are explained in the following paragraphs.

According to the Government of India Act, Article 26, the Secretary of State in Council, has, in the beginning of

May, to lay before the Parliament the account of estimated revenue and expenditure for the current year of the India Office, the High Commissioner, the Central Government, and the Provincial Governments. But these estimates are not discussed or voted upon by the House of Commons. The British Parliament does not exercise any direct control over the financial administration of India, except that no money can be spent on military operations beyond the Indian frontiers without the consent of the both Houses of the Parliament; but as such operations are generally undertaken for Imperial purposes, this condition is of no practical importance. The salary of the Secretary of State, the Parliamentary Under-Secretary, and the contribution by His Majesty's Treasury towards the general administration of the India Office establishment being chargeable to the British Exchequer, are included in the British estimates, and voted upon by the House of Commons. The estimated expenditure of the India Office is included in the detailed estimate of the Central Government and is partly subject to the vote of the Legislative Assembly. The estimate of the amounts required for the maintenance of the office of the High Commissioner is also laid before the Parliament, but it, together with the estimate of expenditure incurred by him for purchase of stores, etc., is included in the detailed estimates of the Central Government. Separate demands are submitted to the Assembly in respect of the votable expenditure of the India Office and the High Commissioner. The absolute character of the supremacy of the Parliamentary control has been asserted a number of times, and been definitely emphasized in the famous Declaration of August, 1917, but as regards the financial administration of India, it has, almost always, been "a sleeping guardian of Indian interests" and the "subtler springs of action" to which the authors of the Joint Report refer, have been aroused only when India's fiscal needs made the increase of cotton duties necessary, and Lancashire raised a hue and cry against it. The Reforms have made no difference. The expenditure, which

is not submitted to the vote of the Central and Provincial Legislature, is practically determined by the Indian Governments subject to the control of the Secretary of State in Council, and does not require the consent of any Legislature.

The budget of the Central Government is introduced in the Legislative Assembly by the Finance Member with a speech which has been referred to already, in which he gives a comprehensive survey of the financial situation, reviews the economic conditions which have a bearing on the public finances, explains the variations of the revised estimates from the budget estimates of revenue, expenditure, and ways and means, and places before the House the programme of expenditure, both on revenue and capital account, and his proposals for financing it with income derived from taxes, loans, and other sources or revenue. In the Council of State the budget is introduced generally by the Finance Secretary. The date on which the budget is introduced in either Chamber is fixed by the Governor-General. For the first three years of the Reforms, the budget was introduced on the 1st March. The budget for 1924–25 was introduced on the 29th February to suit the convenience of the business community. The day on which the budget is introduced, there in no discussion. The members are given time to digest its contents, and formulate their views thereon.

A few days after the introduction of the budget begins its consideration by the Legislature. In the first stage of the budget the members are required to confine themselves to the discussion of the budget as a whole, or any question of principle involved therein. The heads of expenditure which are not submitted to the vote of the Legislative Assembly are not open to discussion, unless the Governor-General otherwise directs, but a convention has grown up during the four years of the Reforms, that this vote is removed by the special message of the Governor-General communicated through the President. The members are then at liberty to discuss the general principles

of all heads of revenue and expenditure. The remarks offered in the course of the debate cover a very wide range and show, as Malcolm Hailey once put it, that the Assembly has all the high explosive ammunition. The general tenor of the speeches delivered by the different members is necessarily determined by their political views, but it is a little unfortunate that in the discussion of the budget the financial aspect of the question does not receive the amount of attention which it deserves and the political considerations, important as they are, are given undue prominence. Finance is not a matter of arithmetical figures ; in them are buried questions of high politics which at once come to the surface as soon as an attempt is made to know what they mean : and in the present political atmosphere of the country, it is almost inevitable that the political aspect of all government measures should have an overshadowing importance. But making due allowance for all these considerations, it cannot but be regretted that most of the speeches delivered in connection with the general discussion of the budget do not reveal a desire to approach the points at issue from a practical and realistic standpoint. The most distinctive characteristic of these speeches is their ornate and extravagant diction. Arguments of value lose their force on account of the members straying into the region of the hyperbole. Gokhale was dreaded as a critic of the financial policy of the Government of India by the Treasury benches, in spite of the practical helplessness of the Legislature at that time, because he spoke from a conviction arising out of the mastery of facts and appreciation of the essentials of the financial situation. His every word was well-selected, and suited to the scale of thought which he sought to express. It is not given to many to attain Gokhale's eminence in style or possess the perfect happiness of expression, or clarity of form. But the budget discussions will be more useful and instructive, if the members' phrases were a little less highly coloured, and used more with reference to the facts of the budget under consideration than to the arguments, whose

intrinsic soundness does not save them from becoming ineffectual on account of their untimely reiteration. The "crying scandal" or the "octopus" of the military expenditure, the iniquitous character of the salt tax and the cotton excise duty, the need of setting up the Indian scale of expenditure and the Indianization of services are all matters the gravity of which is not enhanced by the habitual waste of words in which quite a number of members indulge. Their missiles would be more effective if their points were made sharper by ideas derived from a searching analysis of the figures, which, as already explained, are so arranged as to enable the members both to have a synthetic view of the financial situation, and push their enquiries as far into detail as they may desire. There is room for improvement in the manner in which the estimates are presented, but the members cannot complain that their inability to hit the mark is due to the information being withheld from them. It is sometimes contended that a week is far too short for the examination of the five bulky volumes in which the information is contained. That is obvious. But the members who want to excel as the financial critics of the Government policy, cannot realize their ambition, if a week is all that they can devote to the study of the financial statistics. It is no wonder that they find themselves at sea, if their contact with them for the year begins and ends in the budget session of the Assembly. They require a longer and a more sustained study, if they have to be fully understood. The volumes of estimates retain a similarity of character from year to year. A member ought to come well-equipped for the work of financial criticism by cultivating the habit of gloating over these volumes before the session begins and acquiring a thorough familarity with their details and significance. The variations of the budget proposals of the year from the facts of the previous years are made conspicuous in the detailed estimates and their financial effects and the principles underlying them can be readily understood by an experienced student of these volumes.

The time allotted for their study during the session can, with advantage, be increased, but it is not possible even then to take an intelligent part in the discussion or offer a really well-informed criticism without taking pains to become fully conversant with the nature and the history of the financial policy of the Government in the previous years. The study of the financial questions is in all countries an arduous undertaking, and requires years of laborious and patient work. All the members of the Legislature cannot be expected to have the opportunities or the aptitude for this pursuit, but much good cannot come out of the enlargement of the financial powers of the Legislature unless among the members there are some who make the study of the financial problems their special concern. The Finance Member, after the members have had their say, has the right to reply, in which he further explains, and justifies the policy of the Government in the light of the remarks made by the members in the Assembly. The general discussion of the budget also takes place in the Council of State. The constitution of the Chamber, being less democratic, the speeches are pitched in a lower key than those in the other House, but it cannot be said that they are more illuminating or free from overstatements on that account. There are exceptions in both the Houses, but the general level of the budget speeches cannot but cause some concern to those who expect greater efficiency in the financial administration as a result of the devolution of wider financial powers on the Indian Legislature. From the point of view of the Government the general discussion of the budget helps them to anticipate the lines from which their policy will be attacked in subsequent stages, and to prepare in advance to parry the blows as best as they can. The experience of four years shows that they are quite capable of holding their own in these contests.

The second stage is meant for discussing the details of the budget and granting money for specific purposes. Certain heads of expenditure, commonly called the non-votable items, are not submitted to the vote of the

Legislative Assembly—the most important among them being the military expenditure.[1] For others the proposals are formulated by the Governor-General in Council, and the Legislative Assembly is asked to vote supplies—viz. to grant money for them. Each proposal, as already stated, is called the Demand for Grant and generally relates to each important department of the Government of India.[2] The members of the Legislative Assembly cannot, on their own initiative, introduce a proposal for incurring expenditure. Such proposals must come from the Governor-General. The members can reduce a demand or reject it. They cannot increase it, or, to use the words of the Act, change its destination, which is taken to signify that they cannot demand that the money asked for one purpose be used for another. This is an important limitation of the

[1] The following heads of expenditure are not submitted to the vote of the Assembly:

(*a*) Interest and sinking-fund charges.
(*b*) The amount, the expenditure of which is prescribed by or under the law.
(*c*) The salaries and pensions of persons appointed by or with the approval of His Majesty or by the Secretary of State in Council.
(*d*) The salaries of the Chief Commissioners and the Judicial Commissioners.
(*e*) The expenditure classified by the order of the Governor-General in Council as: (1) Ecclesiastical, (2) Political, (3) Defence.

The words "appointed by or with the approval of His Majesty or by the Secretary of State in Council" are interpreted as under:

(1) All appointments made in England prior to the 23rd December, 1919—the date of the passing of the Government of India Act.
(2) From the 20th July, 1920, the appointments in England may be made by (*a*) the Secretary of State in Council, (*b*) an agent of the Secretary of State in Council, (*c*) the High Commissioner contracting on behalf of the Governor-General in Council or the Provincial Government.
(3) All appointments both before or after the passing of the Government of India Act are assumed to have been made by an authority in India unless there is a definite evidence to show that the Secretary of State specifically appointed the particular person.

[2] Each demand is generally introduced by the Member of the Governor-General's Council in charge of the subject in the following form:

"That a sum not exceeding Rs. . . . be granted to the Governor-General in Council to defray the charge which will come in the course of payment during the year ending the 31st March, 19 . . . in respect of . . . (the name of the department)."

financial powers of the Assembly, and its *raison d'être* is discussed in another paragraph. The power to reduce or refuse the grant is a powerful weapon. The demand can be refused only for one purpose—to put on record an emphatic protest against the general policy of the Government of India, and denounce the fundamental principle of their administration. This has been done in several cases, and the legitimate character of this procedure as a means of expressing the extreme dissatisfaction of the people with the Government's conduct of affairs cannot be questioned. The proposal for the reduction of the grant may have one of the three objects in view. The reduction proposed may be nominal, and the purpose in view may be to elicit the information from the member-in-charge of the department concerned on a particular point. This having been done the motion is withdrawn. The other object of the proposal for nominal[1] reduction of the amount asked for may be to pass a vote of censure on the administration of the department itself. When the motion is brought forward with this object, it is, of course, carried, if the mover can command a majority in the House. The third object of the motion for the reduction of the grant may be the desire to enforce economy in the expenditure of public money. This object can be realized either by proposing reduction or the omission of the particular items shown in the detailed estimate, or moving a reduction in the total grant. In pro-

[1] In the budget debate of 1923 a point was raised as to whether discussion of a non-votable item could be permitted on motions of nominal cuts relating to the votable items; and the President on the suggestion of the Home Member gave a ruling that the members could discuss the non-votable questions on the motions for nominal cuts in the votable items. The members have, however, in the past gone further. They have reduced the demands for votable expenditure to use the cuts as a lever upon the Government to transfer it to the non-votable items. The constitutional position as far as this aspect of the matter is concerned admits of no doubt. As the Finance Member explained, when the Assembly reduces the demand by a particular amount the Government has to keep the expenditure on the votable item within the amount voted by the Assembly. It may, if it chooses, effect economies in the non-votable expenditure, but if it wants to spend the original amount on the votable items, it has to come before the house with a demand for a Supplementary Grant.—*Vide* the Report of the Legislative Assembly Debates for the 14th March, 1923, pp. 3373–8.

posing such reductions the members, for obvious reasons, are at a disadvantage when they have to make out a case for economy in the estimates of the particular departments. That is so in all Legislatures. As E. Hilton Young has well put it, "Men contending for economy in general are always at a disadvantage when pitched against men contending for expenditure in particular."[1] The members, of course, can move a general reduction of the grants, as was done in the Legislative Assembly in 1922. But this method is undiscriminating and does not take into account the actual facts of the situation. It may be used when no other alternative is possible and the need for reduction of public expenditure imperative. That necessity, however, does not alter the unbusiness-like character of this method of making cuts. Notice of a motion to omit or reduce any grant has to be given two days before the day appointed for the discussion of such grant. The Governor-General allots every year a certain number of days for the discussion of demands for grant. The maximum number of days which can be so allotted is fifteen, though in practice about six days are set apart for the purpose. Of these days no more than two can be spent in the discussion of any one demand. If certain demands have not been considered till the last day of the days allotted for the purpose, the President takes steps for the summary disposal of all outstanding matters in connection with the demands for grant. These unconsidered demands are practically voted upon without debate. This process which is usually referred to as "Guillotine," makes the detailed consideration of about sixty-five demands practically impossible. Their discussion gives publicity to the financial operations of the Government of India and enables the members of the Legislature to raise certain issues of broad policy. But they cannot do much in the way of effecting substantial reductions in the public expenditure. This inability of the Legislature to affect the expenditure even in matters which are subject to its vote suggests the necessity of

[1] "The System of National Finance," by E. Hilton Young, p. 92.

devising some means of strengthening its financial control. This aspect of the question has been further considered in the concluding paragraph of this chapter; the Council of State does not deal with the demands for grants. Voting supplies is the exclusive privilege of the Lower House.

The Governor-General in Council has got the power of treating as sanctioned any expenditure which has not been voted by the Legislative Assembly, if he is satisfied that the expenditure is necessary for the discharge of his responsibilities for the good government of the country. The reason for arming the Governor-General in Council with reserve powers may be stated in the words of the Joint Report: "The power to refuse a vote or to refuse to grant the resources required for it (Government) paralyses the Government's hands. In the hands of a Legislature which practically chooses its own executive, such power is natural and appropriate. It affords a convenient and very effective means of making the Government conform to the wishes of the Assembly. Supplies are not refused unless the Assembly wishes to change the executive. But so long as the executive remains nominated and irremoveable, it must be in a position to secure the money necessary for its essential purposes." The Joint Committee wanted it to be understood that the power of the Governor-General in Council for restoring a reduced or refused grant was real and meant to be used when and if necessary. From the point of view of the Government, which is not responsible to the Legislature, the retention of this power in its hands may be justified; but the possibility of its use makes the voting of the demands much less significant as far as the Legislature is concerned, and is not likely to engender the sense of responsibility to which the authors of the Report attach so much importance. The Governor-General has also got the emergency power to authorize expenditure, which may in his opinion be necessary, "for the safety or tranquillity of British India or any part thereof," and according to the official interpretation, it is to be resorted to when the Assembly is not

in session, and the occasion arises which makes it necessary for the Governor-General to incur the expenditure for the safety and tranquillity of British India.[1] The action taken by the Governor-General in exercise of this power cannot be questioned by the Legislative Assembly, and is merely reported by the Finance Member for the information of the House.

It has already been stated that the Legislative Assembly, though it has got the power to eliminate or reduce the budget proposals, cannot increase them or introduce new ones. It has been further provided that it is not lawful, without the previous sanction of the Governor-General, to introduce in either chamber any measures imposing a new charge on the revenues of India. These provisions have the appearance of having been inserted in the new constitution for circumscribing the use of the financial powers by the Legislature. They may have that effect, but their essential purpose is different. The procedure is based on the procedure of the British Parliament. The House of Commons, in spite of the fact that it has the constitutional authority, has voluntarily enacted rules according to which it refrains from initiating proposals for the expenditure of money. It, as a matter of fact, goes further, and does not exercise the power to modify the expenditure proposals of the Ministry, except in so far as such modifications are formally accepted by the latter. This self-denying ordinance of the House of

[1] Referring to the Section 67(8) of the Government of India Act in which the use of reserve powers has been provided for, Sir Malcolm Hailey, in his speech on the resolution moved by Dr. Nand Lal in the Legislative Assembly recommending the circumspection of the use of reserve powers said: "Fortunately or unfortunately, the Assembly is not continuously in session throughout the year. Were the Assembly to continue to be in session throughout the year, there would be no occasion of resort to sub-section 8. But it may arise when the Assembly is not in session, and the expenditure has to be incurred. There are long intervals of time when the Assembly is not sitting and events may then occur which may affect the safety or tranquillity of British India. It is not possible to call a sudden meeting of the Assembly, and the Governor-General in those cases takes the place of the Assembly and authorizes the expenditure of money."—Report of the Legislative Assembly Debates, Vol. III, p. 4457.

Commons is, in the opinion of a number of students of the financial systems of the world, a very salutary feature of the British financial system. It is, besides, the Treasury control and independent audit, the corner-stone of the British system and its excellence is in no small measure due to the existence of this constitutional practice. In those countries in which the Legislature possesses and exercises complete financial initiative, the financial administration has been characterized by extravagance, waste, and misapplication of public funds to an extent as to amount to a national scandal. The Appropriation Committees in the United States of America and the Budget Committee in France, which are the committees of the Legislature, have got the power to eliminate or reduce items and even to increase them or introduce new ones. The balance of the budget, which depends upon each proposal being considered in relation to others and assigned its relative importance in the whole scheme of national finance, cannot be preserved on that account. The departmental officers, whose estimates have been cut down by the heads of the departments or even the private individuals who have got interests of their own in the adoption of particular proposals, can have access to the members of these committees and with sufficient wire-pulling have the budget proposals changed to suit their own ends. These committees do not know the real needs of administration, and on account of their highly technical character, the changes that they introduce are often ill-considered and not co-related to one another. On the floor of the House, the members can move any amendments, which, in America, can, on account of the nature of the constitution, be carried in spite of the known opposition of the Government. The members representing particular districts have the interest of those districts at heart, and can, through the vicious practice of log-rolling under which the members agree to support the proposals of their colleagues in return for the latter's support of their own measures, secure action favouring their own districts at the expense of the general

welfare. On account of this state of things the Treasury in America does not perform any co-ordinating function. The estimates there are merely a collection of departmental estimates, and do not embody any policy or programme. The result from the point of view of the national finances is extremely unfortunate. There is no unity in the financial administration of those countries. The public purse is handled in a haphazard manner. The national point of view is often relegated to the background in the financial affairs. There is a diffusion of responsibility, and inefficiency is the marked characteristic of their financial systems. All these evils arise because the Legislature not only criticizes and checks the financial policy of the Government, but also tries to direct and control it in matters of detail. In India the problem is different. The Legislature cannot relinquish its right to reduce or refuse grants. The control of the purse round which the political struggle has centred in democratic countries has still to be won in India. The time when this weapon will be allowed to "rust in the arsenal of constitutional laws" is still distant. The present expenditure is far too high for the capacity of the nation to bear it, and the traditions which have been built up so far, do not, in spite of their admitted merits, make for economy in the public administration of the country. It may be true that "economy," to quote Lord Bryce, "which was expected to be among the strong points of democracy, has proved to be its weakest," but the Indian Legislature must reduce the present scale of expenditure if money is to be found for our most pressing needs. But in spite of all these considerations, it would not be a sound policy to let our Legislatures initiate proposals for expenditure. It would destroy the concentration of responsibility which ought to be a vital feature of all financial systems. In India, where the local and the particular interests are still strong, and will remain a living factor in our national life for a long time to come, it is and will be highly necessary to keep them in check by making the executive responsible for the formulation of

our financial policy. It may handicap the members in the attempts to provide public funds for the material and moral progress of the nation, but in view of the serious consequences which we know from the experience of other countries arise from allowing the members of the Legislature to have the right of financial initiative, it is worth while to exercise a little patience and let the power of recommending appropriations remain in the hands of the executive, in spite of the fact that it is neither national in personnel nor in spirit. It is the price which we have to pay for building a sound tradition for the future.

The amount voted in the budget for a particular department is the limit beyond which the Government of India ordinarily cannot go without obtaining the assent of the Legislature. But it is obvious that as the estimates of expenditure are framed months before the expenditure is incurred, these amounts are likely, in certain cases, to be found insufficient either on account of underestimating of expenditure or because a need has arisen which could not be anticipated when the budget was passed. In order to provide for these two contingencies the Government of India presents to the Legislative Assembly in respect of those items for which its vote is necessary, demands for supplementary grants, which are dealt with in the same way by the Assembly as the demands for the original grants. The necessity for making a provision of this kind is evident, otherwise the alternative, as Sir Malcom Hailey pointed out in one of his speeches in the Assembly, is "to conceal among the innumerable items which make up one budget a liberal provision of reserves" which would defeat the scrutiny and defy the criticism of the House. That would, besides being dishonest, exempt the Executive from the necessity of asking for the sanction of the Legislature for defraying additional expenditure. But the practice of submitting supplementary estimates, if not properly guarded against, has some dangers of its own. It is possible that the Executive knowing that they can get more money in this way, after the budget has been passed, may

habitually underestimate either because they are careless or because they want to obtain the sanction of the Legislature for some vulnerable items of expenditure, by getting it through in instalments. The supplementary estimates as a means of correcting inevitable errors are necessary, but if they are used as an instrument for evading the vigilance of the Legislature or redressing the results of shortsightedness of the estimating authorities they are then put to uses, which, it goes without saying, are illegitimate. The budget ought to be a comprehensive document in which the public needs are stated in full and in a balanced manner; and when demands are voted upon, each one of them ought to undergo what Stourm calls a competitive examination on its own merits and money provided for it according to its relative importance. This cannot be done in case of supplementary estimates which, if they are made use of as an ordinary means of getting money from the Legislature, are, on that account, likely to upset the budget equilibrium and make the judicious selection of the most important items of expenditure practically impossible. These weighty considerations are of special importance at this stage of constitutional development of our country, and should point to the need of guarding this avenue for obtaining the sanction of the Legislature for expenditure with very great jealousy. The Legislature should, before it accords such sanction, satisfy itself as to the adequate reasons which account for the demands not having been included in the original estimates, or the urgency of the circumstances which make their subsequent presentation to the Legislature absolutely necessary. An examination of the way in which these demands for supplementary grants have been dealt with during the four years of the Reforms makes it necessary to lay further emphasis on the need of making a very sparing use of this method of obtaining legislative sanction. In several cases demands which could easily have been included in the original estimates have been submitted in the supplementary ones. The reasons as to why their

consideration could not be postponed by a few months have seldom, if ever, been given. There are cases in which the demands definitely reduced in the original estimates have again been submitted to the Assembly on no other plea than that of securing the reconsideration of the whole matter even when no new circumstances had arisen which made the adoption of such a course necessary. The examination of the estimates by the Assembly is already none too thorough and the undiscriminating use of demands for supplementary grants is likely to make it less so. It need not be added that additional expenditure should not, except in cases of absolute necessity, be incurred unless a supplementary grant has been actually voted. The violation of this rule, unless there are really extenuating circumstances, must be made a subject of emphatic disapproval.[1]

In a few cases the amount granted by the Legislature for a specific purpose may be exceeded and the fact remain undetected till after the expiry of the financial year. That such occasions should be exceedingly rare in a well-conducted system of financial administration is a primary condition of the control of Legislature over the finances of the country. In the United Kingdom such excesses are regarded as, to use the words of Sir Basil Blacket : " heinous

[1] The rejection of the Ministers' salaries by the Bengal Legislative Council, and the tangle of law-suits which arose out of the action taken by the Government in order to re-submit the vote to the Legislative Council as a demand for supplementary grant has resulted in the formulation of the new rule, according to which a demand reduced or refused by the Legislature can be re-submitted to it for its fuller consideration. Whatever may be said in favour of this rule from the political standpoint, it is unsound from the point of view of preserving the unity and equilibrium of the budget, and its frequent use will impair both and become a source of considerable confusion.

In this connection instruction issued by the Government of Bihar and Orissa in their Finance Department to their estimating officers and embodied in para. 73 of the Bihar and Orissa Budget Manual is worth quoting :

" The supplementary demands are undesirable, in principle, and a free resort to them inevitably leads to laxity in budgeting and control. Their admissibility, apart from the question of the actual provision of funds, will, therefore, be closely scrutinized. The finance of the provinces can be fairly allotted when a reasonable forecast of the resources available can be framed, together with a comprehensive statement of Govern-

offences," and their occurrence discountenanced by the Parliament. They are not taken into consideration unless the matter has been carefully investigated by the Public Accounts Committee of the House. According to the Indian Legislative Rule, No. 49, when the money has been spent on any services for which the vote of the Legislative Assembly is necessary during any financial year in excess of the amount granted for that year, a demand for the excess is to be presented to the Assembly by the Finance Member and dealt with in the same way by it as if it were a demand for grant. The first time that the provision for what is technically called "excess grant," was utilized showed that total amount by which the actual expenditure exceeded the voted grants was rather strikingly large. The Finance Member, admitting the fact that the number of heads under which excess had occurred, called for an explanation, accounted for it by pointing out that 1921–22, the year in which the excesses had occurred, was the first year during which the system under the Reforms of voting on demands for grant by the Assembly came into force and both the Assembly and the Government were new to the system. The explanation was accepted and irregularities condoned by the Assembly.

ment *in all its departments*, in other words, at the time of the budget. The justification for a supplementary demand shall, therefore, rest upon circumstances which are exceptional.

These considerations are independent of the equally important question of the provision of money involved. Under the Devolution Rule 21, even if the provinces possess balances, notice has to be given to the Government of India of the extent to which it is proposed to draw them. It is possible to make budget provision for likely supplementary demands, which, given the circumstances of provincial administration, are to some extent inevitable. But that provision will be of a moderate amount. Apart from it, there remain re-appropriations from savings and the possibilities offered by unexpected windfalls under the revenue heads. But neither of these two contingencies are certain, nor can they be accurately estimated until towards the close of the year, when ordinarily supplementary grants can with difficulty be spent even if sanctioned. All departments should therefore understand that the proper time for the formulation of demands is when the budget is under preparation, and they have an opportunity of stating their fresh requirements. It is not safe to count upon supplementary grants in order to make good matters overlooked at the time of the current budget or to anticipate demands which should properly be preferred in connection with the ensuing budget.

But the exceptional nature of the circumstances, which explained their occurrence, also showed their abnormal character and laid bare the fact that they should not be allowed to become an ordinary feature of the financial administration of the country. If the voting on the demands for grants is to have any meaning in a financial system, the amount voted should constitute the limit of expenditure by the executive, which can be exceeded only under the stress of really compelling circumstances.

The Legislature, though it accords sanction only to a part of the total expenditure of the Government of India, has a complete control over the methods of raising revenue. The revenue proposal of the Government of India are embodied in the Finance Bill, which is an omnibus measure, the object of which is to provide for the continuance or amendment of various statutes, from whose operation the Government of India derive their revenues. Any new source of revenue which the Government of India may want to make use of can, of course, be legalized by insertion in the Bill. The procedure for the enactment of this Bill is the same as that which is prescribed for any other Bill. It can be introduced in either chamber, but the Legislative Assembly is for the purpose of the Finance Bill always the "originating chamber." The revenue proposals of the Government of India are explained in the introductory speech of the Finance Member who, on the day on which the budget is presented, asks for leave to introduce the Bill in the Legislative Assembly. The Bill is also introduced in the Council of State by the Government Member who presents the budget in that Chamber. In the course of the general discussion of the budget the underlying principles of the Bill are commented upon and made the subject of approval or the reverse in both the Chambers. After the demands for grant have been voted upon the Bill is taken into consideration in the Assembly. The motion that the Bill be taken into consideration is brought forward by the Finance Member, and can be opposed by any member of the House. The motion opposing the considera-

tion of the Finance Bill, if carried, means its rejection, and the Government, if this extreme course is adopted, can raise the necessary money only by the use of the reserve powers by the Governor-General. The rejection of the Finance Bill is a legitimate measure when the demands for grant have been completely refused to express the political discontent of the people; but it is not quite logical to authorize the expenditure of money by voting the demands for grant and then throw out the Finance Bill *in toto*, as was done in 1924. If the Finance Bill is taken into consideration, it is discussed and then voted upon clause by clause. Amendments can, at this stage, be moved reducing the rate of a particular tax or its complete remission advocated for two reasons, viz. either because the tax is onerous and ought to be reduced or remitted or because the Legislature wants, by reducing the amount which the Government of India can raise to bring a pressure to bear upon it for reducing that part of expenditure which is not submitted to its vote. After the Bill has been considered clause by clause the Finance Member brings in the motion that the Bill as amended be passed. The Bill having been passed by the Assembly is laid on the table of the Council of State where again the motion is made that the Bill be taken into consideration and then every clause is discussed and voted upon. If the Bill is passed by the Council in the form in which it is sent by the Assembly it is submitted to the Governor-General and is placed on the statute book when it has received his assent. But it may be that certain amendments have been made to the Bill and carried in the Council of State; then the procedure is that the Bill as amended is referred back to the Assembly with the request that it may be agreed to by the latter. If the amendments receive the concurrence of the Assembly the Bill is passed into law when it is presented to the Governor-General for his assent. There is, of course, a possibility that the amendments made by the Council of State will not be accepted by the Assembly or those proposed by the latter be rejected by the Council of

State. An occasion like this when there is an irreconcilable difference of opinion between the two Houses calls for the use of the powers vested in the Governor-General by the Section 67 (3) of the Government of India Act, which empowers him to convene a joint sitting of both Chambers and submit the matter in dispute to its decision. This is the procedure which is applicable to every Bill, but it is of little avail, as far as the Finance Bill is concerned, for finding a way out of the deadlock, as the amendments which give rise to it can be submitted to the Joint sitting six months after its passage in Legislative Assembly. The Government of India cannot afford to wait for six months for the settlement of the dispute. As things are, the Finance Act expires on the 31st March, and the Government of India, on account of the failure of the two Houses to compose their differences, will have to refund any additional taxation that may have been provisionally collected after the introduction of the Finance Bill[1] till the 31st March, and find itself thereafter completely paralyzed for not being able to raise the necessary funds to meet the cost of the administration. If a constitutional crisis of this magnitude is in sight, it is possible that the prospect of having to face it will exercise sobering effect on both Chambers and make them amenable to considerations which may prevent matters from taking their embarrassing course. By formal negotiations, for which there is also a provision, or mutual give and take without them, the Houses may work out a compromise and put an end to the possibility of the situa-

[1] In the Finance Bill a declaration is inserted every year empowering the Executive to levy new rates of customs and excise duties from the date of the presentation of the budget. According to the Provisional Collection of Taxes Act of 1918 a fresh measure of taxation takes effect from the date of its introduction of the Bill. This provision is necessary to prevent loss of revenue to the Government on account of the merchants rushing goods into or out of the country before the higher duties come into operation.

This declaration is deleted when the Bill is passed into law. If the Legislature makes any reduction in the proposed taxes, the amount collected by the Government at the higher rate has to be refunded. The declaration gives statutory effect to the Finance Bill for thirty days, and therefore it is necessary to get it through both the Houses before the end of March.

tion becoming a source of grave inconvenience for all concerned. But it is also possible that the differences between the two Houses may be of a very acute character and not admit of being settled by each House going half-way to meet the other. For a contingency of that kind the present constitution does not provide any way out, except the use of emergency powers by the Governor-General, which may be the last resource of the Executive, when it is about to be confronted with a situation which will leave it without money for carrying on the administration of the country; but it is not a method of establishing harmony between the two Houses of the Indian Legislature. In 1921, when certain changes in postal rates and surcharge upon traffic by inland steam vessels were made by the Council of State which were not acceptable to the Legislative Assembly, it needed all the tact which the Finance Member could command and the forbearance on the part of the members of the Assembly, which was appealed to, by pointing out the necessity of not creating an *impasse* for the amended Bill to be steered through the Legislative Assembly. Since then the events so far have not given rise to conflict between the two Houses on matters of taxation, but the fact that there is no way for ending it, when it does arise in the future, remains a disquieting feature of the relation of the two Houses in financial matters. It has already been stated that the Legislature does not possess or exercise powers of financial initiative in matter of expenditure. The limitation has been definitely imposed in the Government of India Act, and there are valid reasons why it should not be removed. In the Act, and the rules framed under it, however, there is nothing explicitly laid down which may be taken to debar the nembers of the Legislature from putting forward proposals involving increases of taxation. The presidents of the Council of State and the Legislative Assembly have, separately, given rulings which make the proposals for adding to the taxation out of order except on the motion of official members of the Legislature. These rulings have expressly been given on

the basis of the procedure in force in the House of Commons. It is correct that in the United Kingdom all proposals for revenue and expenditure emanate from the Government, but in matters of detailed provisions of revenue there is what E. Hilton Young calls "a wise understanding in the party game," which makes it possible for the Ministry to reconsider, without any loss of dignity, particular proposals of taxation that they may have proposed, and allow it to be revised or substituted provided they are furnished with sufficient funds for giving effect to their financial programme. It is desirable that a similar understanding, tacit if necessary, but well recognized, should grow up in India, which may make it practically obligatory for the Executive to accept any alternative proposals for taxation or revising those brought forward by the Government with regard to which there is a general agreement among the members of the Legislature. The presidents of the two Houses have, in the rulings referred to above, admitted the right of members to suggest the alternative proposals or propose an increase in one item compensated by a corresponding reduction in some other, but they cannot be made effective except on the motion of a member of the Governor-General's Executive Council. The formal right of making a motion may be reserved to the official members of the Legislature, but when opinion in favour of a particular proposal has crystallized itself in the House, the Government should deem itself bound, by constitutional convention, to embody it in the Finance Bill of the year. If this convention is not deliberately fostered, the Legislature will, as Sir Montague Webb has pointed out, have the power of cutting down proposals for revenue or producing deficit without being able to have a controlling voice in the taxation of the country. The questions of taxation are questions in which, according to the tradition and the established practice of the leading democratic countries, the elected representatives of the people claim the special right of having their opinion listened to. India is not a democratic country but, according to the universal agreement of

opinion, it must become one sooner or later. It is well that in the initial stages of her democratic career this right should find a definite place in the unwritten, if not written, constitution of the country. It is convenient to add here that the Legislature does not exercise any control over the estimates of receipts from different sources of revenue. It can determine, subject to the above limitation, the nature and rate of taxation, but the work of estimating the receipts which will accrue from them is wisely left to the executive authorities. It has already been stated that the forecast of revenue is a highly technical business, and its correctness depends upon the knowledge of the complex interactions of the numerous factors, which is only possessed by those who have the necessary opportunities and the data to acquire it. The experts are sometimes wide of the mark, but the uninitiated legislators are well advised in depending upon their trained judgment and criticize and censure them, when experience shows that they have repeatedly failed to read and interpret the correct meaning of the coming events.

It is the fundamental proposition of the present constitution that "the capacity of the Government of India to obtain its will in all essential matters be unimpaired." In matters of expenditure they possess the authority to sanction the expenditure which they consider necessary for the discharge of their responsibilities without the consent or in spite of the definite refusal of the Legislative Assembly. In matter of taxation they have the reserve power of raising funds when the Legislature has turned down their revenue proposal. The latter power is exercised by bringing into operation the Section 67B of the Government of India Act, which authorizes the Governor-General to certify that the passage of the Bill is necessary for safety, tranquillity and interest of British India when either Chamber of the Indian Legislature refuses leave to introduce or fails to pass it in a form recommended by the Governor-General. The Finance Bill being a measure of legislation, it is held that the Governor-General can legitimately make use of

this certification power for raising funds for the Government of India, which the Legislature refuses to grant and which the Governor-General considers necessary for the fulfilment of his responsibilities. The question has been raised whether the authors of the Act intended that the section should be used with regard to the Finance Bill. The interpretation of this section is a matter of law, but it is difficult to see how the irremovable Executive without a majority in the Legislature can carry on the administration of the country without the exercise of this power. "Finance," as the authors of the famous Report put it, "is the vehicle of Government, and unless the Executive can raise money for its needs and lay it out as it pleases it cannot continue responsible for the administration."[1] It can be contended that the present constitution is narrow and does not give sufficient power to the Legislature to influence the financial policy of the Government of India. That is a plea for its early revision; but the exercise of the special power cannot be questioned in view of the fundamental principle of the present constitution. The wisdom of using it in particular cases may, of course, be challenged. The enhancement of the salt tax in 1923 is a case in point, but the Government cannot allow itself to be paralysed when the Legislature throws out the Finance Bill, as it has done in 1924, and leaves it no other alternative for raising funds. It is not suggested that the Legislature may not, under certain circumstances, be justified in throwing out the Finance Bill, but as one well-known Indian publicist has said, that if it is constitutional for the Legislature to reject it, it is also constitutional for the Governor-General to certify it. It is not necessary to add that this power, if the constitution is to be worked in the spirit in which it is conceived, should be rarely used and not be relied upon for imposing taxes, which should ordinarily be imposed with the willing assent of the Legislature. The certification is a counterpart of veto, and we have it from the authors of the Reforms themselves that "the veto

[1] *Vide* the Montagu-Chelmsford Report, para. 165.

is not an instrument of Government, and is tolerable when it is rarely used and does not become obtrusive." The procedure for certifying the Finance Bill is familiar. When the Bill or some clause of it has been rejected by the Legislative Assembly the Governor-General certifies that its passage is necessary, sends it back to that House in the form in which he desires it to be passed, and if the House is not in a mood to accede to his wishes and rejects it again, the recommended Bill is sent up to the Council of State. The Council of State is practically asked to pass it without amendment, and it has done so on two occasions that the Governor-General has used this power. With the present composition of the Council of State or its likely composition under the present constitution, the Government can get it to register its decree. But even if the Council of State insists on making changes unacceptable to the Government, the Governor-General can, on his own signature, place it on the statute book in the form in which he desires its enactment. Ordinarily an Act made by the Governor-General does not take effect unless it has been laid before each House of Parliament for not less than eight days on which the House has sat. But as the Government of India cannot wait in the case of the Finance Bill, it becomes operative as soon as the Governor-General has put his signature to it by the exercise of his emergency powers. It is in reality not an Act in the ordinary sense of the word but an executive order. The extent to which this power is made use of for getting money is the measure of the distance which we have still to travel for making the Indian Government democratic and national.

The statement that the Indian Legislature has, subject to the exercise of exceptional powers of the Governor-General, a full control over the revenue proposal of the Government of India has to be read with one important reservation, and that is that the Legislature has no control over the borrowing power of the Government of India.[1]

[1] The statutory position was thus explained by the Under Secretary of State in the House of Commons:

"The Government of India are free to borrow money in India without

The expenditure from loan funds, like other expenditure, unless, of course, it is specially excepted, is subject to the vote of the Assembly, but actual raising of loans to meet the capital expenditure or any other liabilities which cannot be met from the current revenues of the year, is a matter for the discretion of the Executive Government. The amount, the rate of interest and conditions attaching to the loans are determined by the Government of India with the consent of the Secretary of State in Council, and the Indian Legislature is not required to give its sanction to the amount or terms of the loans. The loans may be raised in England or in India, the rate of interest may be high or low, they may be raised for financing capital expenditure or covering the deficits, the terms offered may be unduly favourable for the foreign investors or be unfavourable as far as the Indian investors are concerned; these and any other matters relating to the loan policy of the Government of India are excluded from the purview of the Indian Legislature. The Legislature cannot initiate any measures affecting the public debt of the country. The proposals of the Governor-General in Council for expenditure relating to interest and sinking fund charges on loans, are not submitted to the vote of the Legislative Assembly. The result is that the Legislature has no means of affecting the loan policy of the Executive in India. This limitation has not attracted any public attention in the country. Public borrowing has far-reaching effects on the economic life of the people. The

any authority of the Parliament. That has been the position ever since the Government of India Act was passed in the 'fifties, and they do of course raise money, in the way the Governments raise money, in India. But under the Government of India Act the money can only be raised in the United Kingdom by the Secretary of State on behalf of the Government of India to such an extent as is authorized by the Act of the Parliament. For this reason ever since the Government of India Act was passed, the Government of India, through the Secretary of State in this House, has come to the Parliament from time to time to get authority to raise money in this country for its future requirements." The Parliament does not by passing the Bill incur any liability on account of the Indian loans, which are raised on the sole security of the Indian revenues. It may be added that the Dominions raise loans in the United Kingdom without any Parliamentary sanction.

State as a competitor for the borrowing capital can, by the rate of interest that it offers, raise the market rate, limit the scope for private enterprise, and dislocate the money market in some other ways. In India the fact that the bulk of public borrowing has till now been done in the English money market has, on account of the increase of our sterling liabilities, been a factor in accentuating our currency difficulties. It is well known that attempts have been made to lay down certain conditions for subscribing to the Indian loans by the foreign investor, which have had the effect of restricting our discretion in spending those loans. Our foreign debt, if allowed to increase indiscriminately, is likely to create serious political complications for the coming generation, which have to be taken into account before we mortgage the future. It is not directly or indirectly suggested that public borrowing should cease or be confined only to India. The Government of India can legitimately increase our public debt for purposes which are distinctly beneficial for the economic development of the country, as our own resources are admittedly inadequate for financing our capital requirements. But there is no justification for exempting public borrowing altogether from Legislative control. The matter has also a constitutional aspect. The Executive can, if it enjoys immunity from the control of the Legislature in determining its loan policy, increase the national burden of public debts without paying due regard to the considerations of economy and the need of keeping the public expenditure within public income. It can always outwit the Legislature, when the latter does not provide funds for certain purposes, by making use of its borrowing powers, more so when all the purposes on which the public money is being spent need not be approved by the Legislature. In England the proposals for raising loans are embodied in a Bill, and do not become operative unless it has, like every other measure of legislation, been passed by the Legislature. If the Indian Legislature is competent to exercise control over the taxation proposals of the Govern-

ment of India, there is no reason why the proposals for raising loans should not be submitted to its vote. The possession and exercise of this power will not make the Government of the country less stable, and will certainly ensure the recognition of the paramount importance of regulating the loan policy of the Government without taking into account any interest other than the need of providing capital for those of our public requirements, the expenditure on which cannot be charged to the revenues of the country. We ought to borrow in the cheapest market, and the terms of the loans should not entail any obligations which a free and self-respecting nation would not like to incur. On account of the historical circumstances, which it is not necessary to explain, the sterling loans raised by the Government of India in the United Kingdom require the statutory sanction of the Parliament. But the loans raised in India are neither subject to Parliamentary sanction nor to that of the Indian Legislature. The Finance Member, in his budget speech, while explaining the ways and means position of the Government of India, gives information as to the amount of the loan which the Government proposes to borrow in England and in India; but that declaration does not bind the Government of India. It considers itself at liberty to make variations from the borrowing programme announced by the Finance Member and, not unoften, does so. It may be admitted the Government of India ought to have a certain amount of latitude in giving effect to its borrowing policy of the year, as it must, as a matter of necessity, be guided to a certain extent by the changing conditions of the money market in England and in India. But the complete exemption of the exercise of borrowing powers from the need for obtaining statutory sanction of the Indian Legislature is an anomaly which can neither be explained by any reference to the necessity of circumstances nor to the transitional character of the constitution under which we are supposed to be living. One of the ways in which the present constitution can be easily expanded, without the revision of the Government

of India Act, is to make the raising of loans in India and in England[1] a matter with regard to which the legislation in India would be considered necessary. It will give to the Indian Legislature a determining voice in shaping the loan policy of the Government of India; of course, only to the extent to which it can effect every measure of legislation initiated by the Executive in India.[2]

It is one of the most important principles of democratic finance that the budget should be voted annually by the Legislature. Certain charges, which for one reason or the other ought not to vary from year to year, may be exempted from the annual vote, but the major part of the public expenditure should be subject to legislative sanction every year. In England there are certain permanent appropriations which are not included in the annual estimates. In India all charges on the public revenues of the country are presented to the Indian Legislature in the books of estimates, but the Assembly is not asked to sanction certain heads of expenditure. But for the other charges, renewal of the sanction of the Legislative Assembly is necessary every year. By this means the whole administration can be brought under review of the Legislature (discussion on non-votable items can be raised by proposing nominal cuts in the votable items) and economy enforced in those spheres which are subject to its direct control. This control, direct or indirect, is partial but can be made use of for extending the influence of the Legislature and narrowing the limits within which the arbitrary powers of the Executive can be exercised. There is nothing in the Government of India Act which may make it necessary for the Executive to require the annual sanction of the Indian Legislature for its revenue laws. The Acts which give the Government of India this authority can remain in force unless amended or annulled. But by a convention, which is now well-established, there is in-

[1] The Government of India Act will have to be amended to the extent of making it unnecessary for the Government of India to go to the Parliament to raise money in the United Kingdom.

[2] The question is further discussed in Chapter XII.

serted in the Finance Act a provision which limits the duration of the Act to one year. It, with one important exception, expires at the end of the financial year to which it relates. For example, in the Finance Bill of 1924 in clause 5 of the statement of objects and reasons it is stated that "the provisions other than mentioned in paragraph 3 (which related to the Tariff Act) will have effect till the 31st March, 1925." The growth of this convention is a great achievement. It recalls to mind the history of many memorable constitutional battles which were fought by the House of Commons in England to assert its right to revise the Revenue Acts every year. In England now, however, only the Income Tax and Tea Duty are renewed every year, and others are permanent; but, on account of complete control of the Parliament over the expenditure and the annual renewals of the two most important taxes, the efficacy of the financial control of the House of Commons is not lessened by the great majority of the taxes being made permanent. In India, to use the words of Adams, "the question of the residence of the control of public policies" being still a subject with regard to which there is and will, for some time to come, be a great deal of controversy, it is necessary to make the revenue laws of the country liable to revision every year. The one exception to this convention is the Tariff Act and the kindred revenue law—the Cotton Duty Act, 1896. The reason for making exception in this case was explained by Sir Malcolm Hailey in his speech, which he delivered in 1921, in replying to the motion of Mr. N. M. Samarth for putting the Finance Act on an annual basis. Sir Malcolm, after stating how embarrassing the annual revision of the Tariff Act would be for the trade, how commitments in advance would not be made, and how the goods would accumulate in the Customs House towards the end of the year in anticipation of any reduction in tariff, went on to say, "My own view is that it will lead to a very great deal of uncertainty on the part of trade if our tariff came definitely to an end at the close of the year and the whole scheme of charges are open to

revision every twelve months."[1] His argument in favour of making the Tariff Act permanent was supported by the representatives of commerce, both Indian and European, and other members of the Assembly waived their opposition to it on being assured that the fiscal policy of India would be submitted to the House for its decision after the question had been thoroughly investigated and reported upon by the Fiscal Commission. In taking that course the members of the Assembly missed the constitutional importance of the conclusion to which they were coming. The question that the Indian Legislature should lay down the fiscal policy of India has nothing to do with the question of confining the operation of the Finance Act to a year. It is one thing to say that the tariffs of India should be protective and another to reconsider the tariff law of the country when other revenue laws come before the Legislature for renewal. It is true that the frequent changes in tariffs increase the speculative character of the trade and make it more of a gamble than it need be. In the countries which have adopted protection such changes have been numerous, and in spite of the fact that in the United States of America the revenue laws are permanent, the frequent changes in the Tariff Acts have had a very damaging effect on the stability of her economic and the integrity of her political life. The Government and the Legislature of India have definitely committed themselves to the policy of protection and, if the shadows which the coming events are casting before, are significant, the policy is not going to be more discriminate—in spite of the insistence on that word of the Fiscal Commission and creation of their pet child the Tariff Board—than the policies which other countries have adopted. The determined efforts at lobbying in advance and the use of other well-known devices, which have been resorted to in all protectionist countries by people who everywhere furthered their private interests under the cover of the public good are going to come. The argument in favour of making the Tariff

[1] *Vide* the Legislative Assembly Debates Report, Vol. I, p. 1257.

Act exempt from annual legislation has little weight in a country where the vast majority of the intelligentsia have an unbounded faith in protection as a specific for the deep-seated economic disorders. With the passage of time the protective movement is going to grow in power and vitality, and the tariff changes will, as a direct result thereof, be frequent and many. The plea of excluding the Tariff Act from annual reconsideration of taxing acts of the Government of India will on that account not be relevant from the standpoint of giving steadiness to our economic life. The more important point, however, is that in the early stages of our constitutional development it is desirable to give to the Legislature a substantial share in determining the taxation of the country. As it is, the Tariff Act is not included in the Finance Bill unless it is proposed to modify or alter it; and according to the ruling of the President of the Assembly, the Acts not recited in the Finance Bill for continuance or amendment are not open to amendment by the House. The members of the Assembly cannot even exercise their admitted right of proposing a reduction in the tariff duties if the Government does not propose any changes in the Tariff Act. It has already been stated that in spite of the fact that in England all proposals for the levy of new tax or for the increase of an existing tax must come from the Ministry, they are subjected to vigilant and well-informed criticism, and the variations are made in response to the opinion with regard to which there is general agreement among the members of the House. The necessity of developing a similar usage has already been emphasized. The members of the House should in practice have the privilege of increasing or decreasing all taxes, including tariff duties, even if in theory they can only reduce them. The conclusion to which these considerations lead is, of course, evident and that is that the Tariff Act should also be reconsidered every year and amended if the Legislature wants to introduce any changes.

The points raised in the preceding paragraph bring us, by a process of natural transition, to the vexed question of

the Indian "fiscal autonomy." It is one of those expressions which gain in richness but not in precision by the frequency with which they are used. It conjures up to the mind of the Indian patriots the vision of a prosperous India, which has been completely ruined by the denial of this inestimable boon by the ruling power, and the grant of that right is in their eyes the master key which will make the revival of economic prosperity possible. But it is possible to detach the question of fiscal autonomy from the passions which it has aroused in the past and understand how matters stand with regard to it in the present constitution. In the widest sense of the word the fiscal autonomy may mean complete financial independence. That right India obviously does not possess. The Indian Legislature does not vote on a substantial part of annual expenditure, and the Indian Government has to obtain the sanction of the Secretary of State for India before it can place its important proposals for incurring expenditure before the Indian Legislature. All revenue proposals of the Government of India have to receive the initial consent of the same authority, and are subject to his veto both interim and final. The phrase, however, is not generally used in that sense. It is taken to mean that either unfettered discretion in revenue matters or, what is narrower still, complete power to regulate our own tariff. Fiscal autonomy in the latter sense, according to the common interpretation of the famous recommendation of the Joint Committee, has been granted to India not by statute but constitutional convention. It was with regard to this power that they said, "Nothing is more likely to injure the relation between India and Great Britain than the belief that India's fiscal policy is dictated and guided in the interest of the trade of Great Britain," and after pointing out such a belief did exist, they stated, "It cannot be granted by statute without limiting the ultimate power of the Parliament to control the administration of India and without limiting the power of veto which rests in the Crown. And neither of these limitations finds a place in

the statute of the British Empire. It can only, therefore, be assured by the acknowledgment of a convention." The convention upon which they relied was the convention of non-intervention on this subject when the Government of India and its Legislature were in agreement with each other. This convention was to be subject to two exceptions. The Secretary of State, according to the Joint Committee, could interfere even when this condition was satisfied, when it was necessary to do so "for safeguarding the international obligations of the Empire or any fiscal arrangements within the Empire to which His Majesty's Government may be a party."[1] It, of course, means that India can, even against her will, be made a party to commercial treaties which the United Kingdom may negotiate with the foreign powers, and to submit to any commercial arrangement which may be devised by the British Government for creating common economic interests among the countries situated in the Empire. The Indian Government and the Indian Legislature will not be able to vary the rates of customs duties which on account of the international or Imperial interests may have to be fixed at a particular level. These are very important limitations of the conventions of non-interference, and if they are ever made effective it will mean revival of the acute controversies which, to put it mildly, will injure the relations of Great Britain and India—the relations which the Joint Committee were so anxious to safeguard. Fiscal autonomy in the limited sense of power to regulate tariffs, which in India has come to mean power to impose protective duties, is possessed by the Indian Legislature, and twice the attempts of Lancashire to repudiate it have been

[1] Sir Maneckjee Dadabhai moved the following resolution on the 22nd March, 1922, in the Council of State:

"The Council of State recommends to the Governor-General in Council that in future India shall not be made a party to any treaty arrangement involving fiscal obligations and international trade relations unless the Indian Legislature has had the opportunity of pronouncing on the same.

The Government pointed out that it was impossible under the present constitution for the Indian Legislature to possess the powers asked for in the resolution. The resolution was withdrawn."

foiled. It is, of course, presumed that agreement between the Government of India and the Legislature will be a normal feature of our public life in matters of tariff policy. This presumption is justified by the past events, though the possibility of divergence is not inconceivable in the future.[1] But from the constitutional point of view it is of greater importance to take the fiscal autonomy to mean the power to control the whole system of taxation in the country. The Secretary of State will, if this power is conceded, forego his right of having all the taxation proposals of the Government of India submitted to him for approval—a right which was so emphatically asserted by Lord Salisbury in his important despatch addressed to the Government of India under Lord Lytton in 1896, and which his successors have ever since exercised. Taxation according to the jurists is an attribute of sovereignty. India cannot have fiscal autonomy in this sense without having complete political autonomy. That is the theory of the matter. But as it has been stated already, if the Government of India Act is to be worked in the spirit in which it is conceived, it will be necessary that not only the Secretary of State but also the Government of India should let the Indian Legislature have in practice the last word in matters of taxation. The funds which the Indian Legislature provides for carrying on the administration should be adequate, but the methods of raising them should be left to the Legislature itself. The power of initiative which the Government of India possesses should be exercised to embody the proposals, which commend themselves to the Indian Legislature, in the Finance Act of the year. The power of final veto may rest with the Crown which, of course, means that the Secretary of State may overrule the Indian Legislature, but this power will in course of time come to be forgotten by the continuous

[1] The difference between the Government of India and the Legislative Assembly on the question of the foreign capital which recently arose in connection with the Steel Protection Bill and had to be composed by a compromise, may be taken as an illustration of what may happen in the future.

practice of non-intervention. This would be real fiscal autonomy, whether statutory or conventional is a matter of no consequence. It is not necessary to add, after what has been said about the control exercised by the Secretary of State in the financial matters of India, that the Legislature has not been given this power in the present constitution.

The Indian Legislature comprises the Legislative Assembly and the Council of State. It is an important question whether the two Houses should in financial matters, as they do in others, possess co-ordinate powers. Their present position is clear. The budget is introduced in both Houses. The general discussion takes place in both Houses. The demands for grants are submitted only to the vote of the Legislative Assembly. The Council of State has nothing to do with granting the supplies. The Finance Bill is introduced, taken into consideration, and discussed clause by clause in both Houses and cannot, like other Bills, be deemed to have been passed by the Indian Legislature unless it has been agreed to by both Chambers, either without amendments or with such amendments only as may be agreed to by both Chambers, though it is initiated in the Legislative Assembly. It has already been pointed out that if the agreement between the two Chambers cannot be reached before the 31st March, the situation is likely to become piquant in the extreme and can only be eased by the exercise of the emergency powers by the Governor-General. The question as to whether the Council of State has or ought to have any power over the Finance Bill has been thrice raised in the Legislative Assembly. Twice it having cropped up more or less like a side-issue was shelved. In 1923 it was definitely brought up in the form of a resolution.[1] The motion that the Council of State should not

[1] The resolution was moved by Mr. N. M. Samarth on the 12th July, 1923, and ran as follows:

"The Assembly recommends to the Governor-General in Council that effect be given, by the amendment of the Government of India Act if necessary, to the statement of the Joint Parliamentary Committee that they have so constituted the Council of State as to be a 'true Second

have the power of amending the Finance Bill, which must always originate in the Legislative Assembly, was thrown out by a narrow majority of five, all the official votes, of course, having been cast against it. It was contended by the non-official members who supported the motion, that it was against the intention of the Parliament that the Second Chamber should have any power over the money bills. This argument was challenged by the official spokesmen and it was stated that there was nothing in the Government of India Act or the report of the proceedings of the Joint Parliamentary Committee to lend colour to the view. But both official and non-official members went further and discussed the proposition on its own merits. The official view was that the existence of a Second Chamber with full powers in money as in other matters would ensure the harmonious political development of the country, hasten the process of the transference of the supreme power from the Parliament to the Indian Legislature, and afford scope for eminent men of ability and experience to give the benefit of their advice and guidance in all public matters in the more tranquil atmosphere of the Upper

Chamber' by making it obligatory to observe in practice the following principles:

(1) Bills imposing revenues or moneys or imposing taxation or containing provisions incidental to financial arrangements for the year shall originate in the Legislative Assembly.

Provided that a Bill shall not be taken to fall under this category by reason only of its containing provisions for imposing or appropriation of fines or other pecuniary faculties or for demand or payment or appropriation of fees for licenses or fees for services under the law proposed therein.

(2) The Council of State may not amend any Bill falling under the category aforesaid.

(3) The Council of State may not amend any Bill so as to increase any proposed charge or burden on the people as voted by the Legislative Assembly.

(4) The Council of State may within the time limit to be laid down by the Legislative Assembly, return to the Legislative Assembly any Bill, which the Council of State may not amend, requesting by message the omission or amendments of any items of provisions therein. And the Legislative Assembly may if it thinks fit make any such omissions of amendments with or without modification.

(5) Except as provided above the Council of State shall have equal powers with the Legislative Assembly in respect of all proposed laws."—*Vide* the Legislative Assembly Debates Report, Vol. I, p. 4616.

House, when they cannot, for considerations of age, stand the strain of work in the more representative chamber. The non-officials, on the other hand, controverted the view and while admitting that the Second Chamber may be necessary even when India becomes a fully self-governing country, they questioned the advisability of conferring on it equal powers in respect of money matters. They pointed to the trend of events in other countries which had assigned a subordinate place to the Second Chamber in all matters, particularly financial, and given the Lower House a decisive voice in purely financial matters. The deadlocks between the two Houses, it was predicted, would occur in the future, and unless timely measures were taken against their becoming very serious, there was no doubt that the will of the people, as expressed through the members of the more democratic chamber, would ultimately prevail. The earnestness with which the subject was debated, shows that whatever may be the actual financial powers of the Legislative Assembly the members have begun to take themselves quite seriously with regard to them. The question being one with regard to which there can be a legitimate difference of opinion, and the solution of which will depend more on the logic of events than on the arguments which may be urged in favour of one view or the other, it is somewhat premature to forecast the future course of developments or lay down the conditions which ought to govern the relations of the two Houses in the financial organization of the country. There is one consideration, however, which needs a certain amount of emphasis in this connection. A Second Chamber which incurs the suspicion of being an organ of the vested interests is bound to lose the confidence of the people. If there is a trial of strength between the two Houses there can never be the slightest doubt that the Upper House, if it is not responsive to the main current of national life, will not be able to resist the pressure of the Lower House. There may be a need of providing safeguards against the democratic haste of the popular chamber. It may be desirable to have

a House which is a "reservoir of special knowledge and refined wisdom." But if it forfeits the general confidence of the people, whatever be its functions on paper, it will practically have very slender powers. Of all ways of constituting the Second Chamber, making it a mechanism of giving effect to the claims of the property-owning classes, is perhaps the least effective. It will thereby become the standing emblem of class differences which the democratic spirit makes increasingly irksome, and a constant challenge to the progressive forces in the community. It, so constituted, will instead of making the political development of the country harmonious, arouse antagonisms and become a rallying-point of the most reactionary elements in the country. If such a chamber possesses full powers in financial matters, things will come to a head very soon and the inevitable sequence of events, which finally will make the Lower House predominant in the sphere of finance, will run its natural course. "The difference in functions between the two Houses," Lord Bryce tells us, "turns chiefly on finance," and that is so because the Second Chambers, almost in all countries, have been dominated by the conservative classes. It may be wrong to commit the financial destinies of India to one chamber, but it cannot be right to give equal finance powers to the Second Chamber when it, instead of reviewing matters from a more elevated standpoint, merely stands for an order of things which every one knows has to pass away. One of the ways in which a Second Chamber can derive authority, which make it worth having, is, we have it from Lord Bryce again, the traditional respect felt for it by the people. It cannot be said that the Council of State in India has during its short career handled public affairs in a way as to build up for itself the traditions which may stand it in good stead in the future. The Council of State in order to be a true Second Chamber that the Joint Committee wanted it to be, has to regulate its conduct of public affairs in a non-partizan spirit and make the people feel that its revising authority rests on the dignity and wisdom which distinguish its

deliberations from those of the Lower House. The most ardent advocate of the Council of State cannot claim for it these distinctive qualities. It does not possess any power of making appropriations, and the power of amending the Finance Bill it will retain only if its composition and the atmosphere in which it does its work undergo a radical change.

There is one point with regard to the public expenditure in India which requires just a passing reference in explanation of the financial powers of the Indian Legislature. India, on account of her subordinate political position, has had, since 1859, to meet expenditure for purposes in which, to quote the words used in the terms of reference of the Welby Commission, the Government of the United Kingdom and of India are both interested. The Government of the United Kingdom being the supreme authority which governs India, there are no purposes for which the money is spent from the Indian exchequer, in which it is not also interested. But the expenditure, which is referred to here, is for those services which are maintained for purposes in which the two Governments are held to have common interest. In the past, charges have been thrown on the Indian tax-payers which, according to the views of various authorities, were essentially unjust, and still there are large amounts under dispute, which are awaiting settlement.[1]

[1] The Financial Secretary, in his speech on the resolution moved by Sir Purshotamdas Thakurdas in the Council of State, admitted that amounts still under dispute are large. Since 1900 some of these charges have considerably increased. To give an illustration the capitation rate —a charge imposed on the Indian revenues for each man borne on the establishment of the British force in India—has increased from £7–10$ (the amount which was considered excessive by the Government of India in 1900) to £25–13$ in 1922–23.

The resolution referred to above was moved on the 16th July, 1922, and ran as follows:

"The Council recommends to the Governor-General in Council that in all matters where the apportionment of financial liabilities between the Government of India and His Majesty's Government, no compromise should be made between His Majesty's Government and the Government of India without the previous sanction of the Indian Legislature. The Council further recommends to the Governor-General in Council that where arbitration is resorted to, the arbitrators of such disputed items between the Government of India and His Majesty's Government should be the Premiers of the Empire in Conference assembled and no body else."

It is not necessary to discuss the justice or otherwise of requiring India to meet these charges; but it has to be mentioned that the Government of India have, in the past, been called upon to find money for purposes which they held to be of no interest to India, or the importance of which, from the point of view of India, did not warrant the amount of contribution on which she was required to make.[1] They protested against such charges in vain and had, in several cases, to admit their utter helplessness in the matter. The Welby Commission was specially entrusted with the duty of investigating the whole question and making recommendations for its solution. The Commission recommended the reapportionment of certain specific charges but they did not go very much further. They approved of the proposal for forming an impartial tribunal[2] for the arbitration of such disputes, though they did not say as to how it was to be constituted. They, however, laid down one general principle, the soundness of which has not been affected by the lapse of time. While recognizing that India was not a distinct political entity, they contended that for securing justice to India, she and England—the two parties to the disputes—should "both be conceived independent of each other, fighting out their case on strict commercial principles."[3]

That was in 1900. Since then the amounts which India has had to share with or pay to the British Exchequer have increased. The political status of India, whatever opinions may be held about the exact position, is now distinctly higher. She is politically more self-conscious, and any act

[1] Reforms have settled the question of the expenditure of the India Office about which there has been much controversy. The salary of the Secretary of State and the Under-Secretary of State and the expenses of his establishment maintained for political and administrative functions are now charged to the British Exchequer; and as the remaining agency functions will also, in due course, be transferred to the control of the High Commissioner, the whole expenditure of the India Office will after some time be borne on the British estimates. The arrangement is fair and no more need be said about it.

[2] The suggestion of constituting an independent tribunal for the settlement of these disputes was first made by Mr. (now Earl) Balfour and later on endorsed by Lord Salisbury.

[3] *Vide* Welby Commission Report, Vol. IV, para. 334.

of inequity is certain to be resented much more keenly than before. India's moral right to be heard in the matter is admitted by authorities of high repute, and no settlement of the question can be satisfactory to which she is not a party. It is not germane to the drift of the argument to examine the specific charges and say how far their apportionment is equitable. But the validity of the arguments in favour of working out an arrangement which may leave no room for a legitimate grievance on this score has become stronger on account of the altered status of India. The Secretary of State and the Government of India, on account of their non-representative character, cannot be regarded as authorities whose concurrence should be considered sufficient for imposing such charges on India.[1] The Indian Legislature should have the power of affecting the settlement of these disputes. The general impression that the English view is advocated with greater success than the Indian can only be dispelled if the Government of India associates itself with the Indian Legislature in the conduct of these negotiations in some acceptable manner. This is the only way in which the suspicion can be completely disarmed. A deliberative body of the size of the Legislative Assembly cannot carry on negotiations in which there must be a great deal of give and take. The best way of doing so will probably be to take the Finance Committee into confidence when the negotiations are going on. There are certain constitutional difficulties in adopting this course. Most of the charges under dispute relate to those heads of expenditure for which the sanction of the Legislative Assembly is not necessary, and to let it have a say in admitting their equity would bring them under its purview. The Government of India is still a subordinate

[1] Referring to the assumption that in the disputes between England and India the Government of India could speak for the Indian people Mr. Gladstone once said: "It appears to me that to make such a statement—that the judgment of the Viceroy is a sufficient expression of that of the Indian people—is the expression of a paradox really surprising and such as is rarely heard amongst us." Time, since these words were used, has made many changes but they have not affected the truth of this observation.

branch of administration and will, in the event of an irreconcilable divergence between the Indian and the English points of view, have to submit to the wishes of the authorities in England. The constitutional difficulties are there, but it is essential, in spite of them, to devise some arrangement which may be based on the recognition of the necessity of convincing the Indian Legislature that no unjust charges are being imposed on India. The present constitution cannot claim the merit of being very logical, and if to its many other inconsistencies one more is added, which will have the result of reassuring the Indian people that they are receiving a fair treatment in financial matters of common interest, it will remove one of the many causes of friction between India and Great Britain. The Inchcape Committee has admitted the propriety of attaching due weight to the view of the Government of India before such charges are finally imposed on the Indian Treasury. That will not meet the requirements of the case. It is the people of India whose views, as expressed through their representatives in the Legislature, should have paramount influence on the settlement of such disputes. It is not necessary to suggest the particular arrangement, which will be adequate for the purpose. The Judicial Committee of the Privy Council was suggested as a suitable court of arbitration by Sir William Wedderburn and Mr. Dadabhai Naoroji in their Minority Report of the Welby Commission. Sir Purshotamdas Thakurdas has suggested that the Premiers' conference is a more suitable body for the purpose. It is immaterial how the tribunal is constituted provided it satisfies the primary condition of enjoying the confidence of the Indian people.

The political evolution of India will itself solve the difficulties in course of time. India, when she has attained the status which will make it possible for her to brook no dictation, will only consent to pay when she can get her money's worth in return. But that is yet a distant event. For some time to come we will have to rely on less satisfactory expedients. So long as there are any charges,

which have to be divided between India and England, it is necessary to satisfy the parties regarding the justice of the division. The constitution of an independent tribunal of arbitration will go a long way in setting at rest the controversies which have created so much ill-will. To stick at the constitutional difficulties and let the thorns rankle is pedantic and shortsighted. It is necessary, therefore, to associate the Indian Legislature in the settlement of these disputes, and make the Arbitration Board an integral part of the financial arrangements of the country.[1]

Estimates in the Provincial Legislatures.—The manner in which the estimates are dealt with in the Provincial Legislatures need not be explained at length, as the procedure adopted in the provinces is very similar to the budget procedure of the Central Legislature. The estimates of revenue and expenditure are laid before the Provincial Legislature in the form of a statement by the Finance Member of the province concerned, with an introductory speech in which he surveys the financial situation of the province. The day on which the budget is opened in the Provincial Legislature is fixed every year by the Governor and varies from province to province. It is generally some day at the end of February or the beginning of March. A few days after its introduction, there is a general discussion of the budget in which the whole policy of the Provincial Government is brought under review and criticized. No motion is made at this stage, nor is the budget submitted to the vote of the Council. The discussion turns round on the budget as a whole or any principle involved therein. It generally lasts for two days,

[1] Sir B. N. Mittra, the Financial Adviser Military Finance, has, since the above was written, been deputed to England to settle points under dispute—especially the question of the capitation rate. The suggestion of Sir Purshotamdas Thakurdas, who since transferred his activities to the Legislative Assembly, that the Indian Legislature may in some way be associated with the conduct of the negotiations, has been unceremoniously rejected by the Government on the ground that it is a matter which only concerns the Executive, and that the latter means to do its business itself. This attitude is, from the standpoint which has been urged in the text, extremely short-sighted and is bound to intensify the existing distrust of the *bona fide* of the Government.

and the Finance Member has the right of reply. The observations made with regard to the quality of speeches delivered at this stage in the Central Legislature can, with slight variations, be repeated with regard to the speeches in the Provincial Legislatures. The political considerations are unduly prominent, and the financial aspect of the budget does not receive sufficient consideration. The counts of the speeches are, for obvious reasons, different, but their general tenor is the same. After the general discussion the next stage is the voting on the demands for grants. The maximum number of days which can be allotted for the consideration of the demands is twelve, but the actual number varies from six to nine. The limitation, which makes it impossible for the members of the Central Legislature to enhance or change the destination of a grant is also operative in the case of Provincial Legislature. No proposal for appropriation can be made except on the recommendation of the Governor communicated to the Council through the Executive Councillors or the Ministers. The proposals for reduction may be nominal, in which case the object is to elicit information or condemn the policy of the department concerned, or they may be substantial, in which case the object is to effect economies in expenditure. The demands can be refused, which extreme step can be justified when the political discontent of the people is acute and seeks expression in a forceful manner. The step may be taken not because the Provincial Government itself is at fault, and does not respond to the demands of the public opinion, but for reasons of all-India character. It is rather unfortunate that the provincial and the national politics should thus get mixed up, but at this stage of the political development of the country, it perhaps cannot be avoided. The demands not voted till the last day of the allotted days can be disposed of in a summary manner, and in every province quite a number of demands are thus passed without discussion.

The characteristic feature of the provincial budget is

that all heads of provincial expenditure are divided into two heads—Reserved and the Transferred.[1] The distinction is based on the distinction between the authorities which control these heads of expenditure. The Reserved heads relate to those services which are in charge of the Governor and the Executive Councillors, who are not responsible to the Provincial Legislatures for the manner in which they discharge their duties. The Provincial Legislatures can influence their policy but not determine it. The transferred heads of expenditure relate to those services, which are in charge of the Ministers, who are elected members of the Provincial Legislature, and responsible to them for the policy and administration of these services. The Governor has been empowered to authorize expenditure in cases of emergency, as may in his opinion be necessary for the safety or the tranquillity of the province, or for carrying on any department. This power he can exercise both in respect of the reserved and the transferred subjects. But the power of restoring a reduced or refused grant, which has also been vested in him, can be used only with regard to the reserved subjects. If a demand for grant for the transferred subject has been reduced the reduction must be given effect to, and unless additional money is voted for the purpose in a supplementary grant, the reduced amount is, under ordinary circumstances, the limit for incurring expenditure on the service concerned. If the demand has been totally refused, either the department must be abolished, or if that will mean paralysis of

[1] The distribution between the Reserved and the Transferred heads of expenditure for the year ending 31st March, 1923, is given in the following table. The proportion between the two heads has not been materially changed since then.

(In crores of Rs.)

Province.	Reserved.	Transferred.	Per cent.
Madras . .	12·38	4·15	R. 75 ; T. 25
Bombay . .	13·30	5·24	R. 72 ; T. 28
Bengal . . .	6·86	3·38	R. 66 ; T. 34
United Provinces .	11·34	3·38	R. 77 ; T. 23
Punjab . . .	10·09	3·02	R. 77 ; T. 23
Bihar and Orissa .	3·39	1·39	R. 71 ; T. 29
Central Provinces .	3·76	1·64	R. 70 ; T. 30
Assam . . .	1·69	·54	R. 75 ; T. 25

some vital public activity, like education, the Governor may, if he so chooses, use his emergency powers and authorize enough expenditure for *carrying on* the service. He cannot restore the amounts necessary for the expansion of the department. The use of the emergency powers can be justified when the demands for grant have not been considered on their own merits, and their refusal is due to reasons, which, whatever their importance, are extraneous to the purpose for which the service is maintained. There is provision in the constitution under which the Governor-General in Council can, with the previous consent of the Secretary of State, practically declare the transferred subjects should cease to be transferred for such period as he may consider necessary. When this is done, the Governor can only be bound by the considerations of expediency in the amount of weight which he attaches to the public opinion in the administration of the subjects committed to the charge of the Provincial Governments. The reserve powers of the Governor are not meant to be used very frequently, though, on account of the growing tension between the progressive political parties and the Government their use may become a matter of every-day occurrence. Certain heads of expenditure are not submitted to the vote of the Provincial Councils, but such heads constitute a small portion of the total provincial expenditure.[1]

[1] The following charges need not be submitted to the vote of the Provincial Councils :

(1) Contributions payable by the Provincial Governments to the Governor-General in Council.

(2) Interest and sinking fund charges on loans.

(3) Salaries and pensions of persons appointed by or with the approval of His Majesty or by the Secretary of State in Council.

(4) Salaries of the Judges of the High Court of the Province and of the Advocate General.

The items 1, 2, and 4 are such that with regard to them no exception can be taken on the score of their being non-votable. The item 3 is important, and its exemption from the vote of the Council is due to political reasons which need not be discussed here.

In 1922–23 out of the total provincial expenditure of about 105 crores, 82·3 crores was voted and 22·7 crores non-voted, or, in other words, about 78 per cent was voted and the rest non-voted. Out of the total non-voted expenditure of 22·7 crores the provincial contributions represented 9·2 crores or about 41 per cent of the total.

The control of the Provincial Legislature over the taxation policy of the Provincial Governments is exercised through their legislative power. In this case again the members of the Provincial Councils cannot propose an increase in taxation or introduce a proposal for imposing a new tax. This must be done by the Government. The control of the Legislature over the revenue policy of the Provincial Governments is not adequate. This is due, in the first place, to the fact that the practice of limiting the duration of the revenue laws to a year has not been introduced in the provinces. In a few cases the new taxes have been imposed for a year, and renewed or rejected after the expiry of that period. But the convention of embodying the most important revenue laws in a comprehensive Bill every year has not been established in the provinces. Any variation in the rates of the taxes needs the sanction of the Councils, but the taxing Acts do not come before them every year as a matter of course. But the more important reason, which accounts for the inadequacy of the legislative control over the revenue policy of the Provincial Governments is the peculiar character of the land revenue, which is the mainstay[1] of the provincial finance. It is an impost which has been called rent or tax, according to the political views of those who have discussed its place in the fiscal system. The officials have been inclined to base the claim of the State to a part of the yield of the land, or its money equivalent on the ancient custom of the country, according to which the land is held to be property of the State, or to use the technical term "State domain," and call the contribution paid by the cultivators of land, or the non-cultivating claimants of its produce, rent due from the tenants to the owner of the land. The Indian writers on the subject have generally taken the other view, and held that land revenue is a tax on agricultural incomes, and a very onerous tax for the matter of that, inasmuch as men of very limited means have to contribute 50 per cent

[1] In 1922–23 out of the total provincial revenue of 75·73 crores land revenue was responsible for 34·92 crores or about 45 per cent.

of their net profits. What is, however, of greater significance, from the standpoint which is being presented here, is that on account of the claim for the payment of the land revenue being based on siegnorial right of the State, the rate of land revenue and its assessment and collection do not require statutory sanction. The Joint Parliamentary Committee has recommended that steps be taken to put the whole land revenue policy on a statutory basis, and bring the imposition of the new burdens within the purview of the Legislatures.[1] In pursuance of this recommendation the committees of the Provincial Councils have been appointed in two or three provinces, but till now nothing has been done to put matters on a more satisfactory footing. The question, it may be admitted, requires very careful handling, but as long as an important

[1] In this connection it is worth while to give an extract from the report of the Joint Select Committee. They said:

"The Committee are impressed by the objection raised by many witnesses against cases in which certain classes of taxation can be laid on the people of India by the Executive action, without in some cases any statutory limitation of rates, and in other cases any adequate prescription by statutes of the methods of assessments. They consider that the imposition of new burdens should gradually be brought more within the purview of the Legislature. And in particular without expressing any judgment on the question whether land revenue is rent or tax, they advise that the process of revising the land revenue assessments ought to be brought under close regulation by statute as soon as possible. The Committee are of opinion that time has come to embody in the law the main principles on which the land revenue is determined, the methods of valuation, the pitch of assessment, graduation of enhancement, and the chief processes which touch the well-being of the revenue payers."

The Decentralization Commission was also of opinion that the general principles of assessment such as proportion of net profits on the land which the Government should be entitled to take and the period of settlement should be embodied in the provincial legislation instead of being left to the executive order.—*Vide* Decentralization Commission Report, Vol. I, p. 95.

In pursuance of the recommendation of the Joint Select Committee, committees of the Legislatures have been appointed in three provinces, i.e. Madras, the United Provinces, and the Punjab, to enquire into the whole question. They have submitted their reports. No action has been taken as yet on the reports in the United Provinces and the Punjab. They are presumably under consideration of the Government of India. In Madras, Land Revenue Bill has been introduced by the Government but rejected by the Legislature, the reason for its rejection being the unwillingness of the Government to place the future enhancement of land revenue on a statutory basis, in spite of the express injunction of the Joint Select Committee to that effect.

source of income of the provinces, like the land revenue, is not subject to the approval and control of the Legislatures, their control of the Provincial Executive is and will remain very unsatisfactory. The Provincial Governments have also the power to vary the irrigation rates without the sanction of the Provincial Councils. The income from forests, being in the nature of the economic receipts, is, of course, not subject to the legislative control. The Provincial Councils are thus, on account of the nature of sources from which the Provincial Governments derive their revenues, debarred from having a controlling voice in the determination of their revenue policy. The position has to be revised in order to make the financial control of the Provincial Councils adequate and comprehensive. The Provincial Governments also enjoy restricted borrowing powers. The expenditure from loans is subject to the vote of the Councils, but the manner of raising them and their terms are determined by the Provincial Governments, subject to the control of the Government of India. The exemption of the provincial loans from the control of the Legislature has even less justification than that of the loans raised by the Government of India, as they are generally raised in India or borrowed from the Government of India.

General Observations.—The distinction between the heads of expenditure which are submitted to the vote of the Legislature and those which are not is a vital feature of the Indian financial system. The figures of votable and non-votable expenditure show that the expenditure, both central and provincial, for which the vote of the Legislature is necessary, bears a much larger ratio to the total expenditure than it is generally supposed.[1] The exclusion of certain items from the vote of the Legislature is not peculiar to India. Even in the United Kingdom

[1] The figures of the provincial expenditure has already been given. About three-fourths of the total expenditure is votable. The figures of the central expenditure under voted and non-voted heads for the year 1922–23 are 127 and 135 crores respectively. That means that about 48 per cent of the total expenditure was votable. In the budget estimates of 1924–25 out of the total estimated expenditure of 209·22 crores about 93·80 crores or about 45 per cent is votable. The total voted expendi-

there are certain charges known as the Consolidated Fund Charges, for which the Parliamentary sanction is not required. But the underlaying reasons, which account for making certain heads of expenditure non-votable in India, arise from the provisional nature of the Indian constitution. "The progressive realization of responsible government in British India as an integral part of the empire" is the ultimate goal of British policy in India, but "progress in giving effect to this policy can only be achieved by progressive stages." The Indian Legislatures having been granted the first instalment of responsible government, it has been deemed necessary to exclude certain charges from their vote, as they are now to their work and have still to establish their competence to deal with them. In the Central Legislature the heads relating to defence, foreign and political, are non-votable. In the Provincial Legislature the most important non-votable item, or at least the one whose exclusion is due to the Legislature being on their trial, is the "salaries and pensions of persons appointed by or with the approval of His Majesty, or by the Secretary of State in Council," which in plain words means that the salaries and pensions of the members of what are known as the Imperial services, whose personnel is mainly European, cannot be submitted to the vote of the Provincial Legislatures. The reason for keeping the military, foreign, and political expenditure outside the control of the Central Legislature is obvious. These are the basic activities of the State and the Legislature, which is learning its work, cannot be expected to appreciate their importance, or be allowed to tamper with them. The continued presence of the English officials being essential "to help India along the difficult journey of self-government," it is necessary that the Indian Legislature should

ture includes the expenditure on railways both on revenue and capital account. These amounts are large, and on account of the shortness of time allotted for the voting of grants the railway expenditure does not receive the amount of consideration that it deserves. It is hoped that now that the railway finance has been separated from general finance, the railway estimates will be presented in greater detail and receive fuller consideration on the part of the Legislative Assembly.

keep their hands off the money required to secure their services. An attempt was made in 1922 to take advantage of the ambiguity of a few words in the Section 67A of the Government of India Act to get the distinction between the votable and the non-votable heads abolished, and bring the whole expenditure under the vote of the Legislative Assembly.[1] Nothing came out of it, as it was clear that the intention of the authors of the Reforms could not be defeated by the mere fact that there could be a reasonable doubt about the interpretation of a few words in the Act, the distinction being one of the safeguards which they have provided to "gain time for the process of growth to occur." In order to make the matter quite regular, the question was referred to the Law Officers of the Crown, who, in due course, gave their ruling that the distinction between the votable and the non-votable heads could only be abolished by the revision of the Government of India Act. The distinction is due to reasons which are inherent in the very nature of the present constitution, and cannot be explained away by the exercise of legal acumen or subtle differences of interpretation. From the point of view of the ardent advocate of the political progress of the country, it is unnecessary and a source of great irritation. From the standpoint of the student of the Indian financial system, it is to be regretted, as its existence makes

[1] The resolution referred to here was moved by Mr. P. P. Ginwala on the 26th January, 1922, in the Legislative Assembly and ran as follows :

"The Assembly recommends to the Governor-General in Council that such steps, as may be necessary, may immediately be taken to abolish the distinction between the votable and the non-votable items in the budget and to submit the whole of the budget to the vote of the Legislative Assembly."

The mover of the resolution contended that the Section 67 (3) of the Government of India Act in which it is stated that the non-votable items are not open to the discussion of either chamber "unless the Governor-General otherwise directs" could be interpreted to mean that it was within the competence of the Governor-General, not only to permit the discussion of the non-votable items but also submit them to the vote of the Assembly.

This view, as it is stated in the text, is incorrect, and the arguments with which the mover and his supporters strengthened their case constitute a piece of political sophistry, which cannot be of any use in advancing the cause of the political progress of the country.

the dispassionate consideration of the financial policy of the Indian Government exceedingly difficult, and arouses suspicions which cloud and warp the judgment of the critics of the Indian finances. But the fact remains that the distinction is part and parcel of the new constitution, and can be eliminated only by accelerating the pace of political progress in India. Its continuance is the result of the belief of our rulers that the people of India are still politically immature, and lacking in some of the essential attributes of the self-governing nations. It is possible to take exception to the belief itself, but if that is taken for granted the non-votable items should be considered a corollary of the fundamental proposition.

The present conduct of affairs by the Legislatures in India is of importance, not merely because they may thereby make the Indian opinion effective in the conduct of the financial business, but also because they are doing a great deal of the pioneer work. Their powers are limited, their attitude towards national finances is affected by a multitude of considerations, their methods are lacking in the definiteness of purpose and sometimes the courage needed to take a far-sighted view of the matter. They have no precedents, and because they have no precedents, it is highly important that they should not create bad ones. The traditions are the props on which the national life rests; and if in the management of the national finances good traditions are deliberately developed, the future generations will look back to the work of the present Legislatures, not from the point of view of what they have achieved, but how they have set about their work. They have to regard themselves, to use the words of a well-known lawyer, "as the outpost sentinels of posterity holding keys of the citadel." The British House of Commons has attained its present position in the financial system of the United Kingdom because of the traditions on which the financial procedure is based. It is very difficult to mend things when a wrong beginning has been made, and the people have got used to it. The old evils have a way of

appearing a part of the divinely-ordained order of things. The problem of having a well-administered system, which in America has baffled solution so far, has arisen because of the loose ways of doing financial business, which have been tolerated there for such a long time, and now appear inevitable. In matters of finance the distant view is the most important. The system that is in the process of development must, besides being efficient, orderly, and well regulated, be adaptable to the ever-increasing needs of a growing democracy. The Legislatures will, in future, be the heart of our political system, and whether our financial system will work well and be responsive to the vital needs of the national life will depend upon them. This is the view which has somehow to be presented to the members of our Legislatures and kept alive in their minds in order that they may not look upon themselves as "ephemeral transient non-entities," but the builders of the future. It is too early to say whether a good beginning has already been made. The view which has come to the fore, of late, is that the present constitution is not only transitional but absolutely worthless. The acceptance of this view obviates the necessity of giving thought to what the Legislatures do now, as they and their underlying principles have, according to this view, got to go. But the need of taking the prospective view in the handling of the financial affairs has been urged on the assumption that a beginning of the Parliamentary form of government has already been made, and the future development of the financial system will be affected by the conventions which the members of the Indian Legislature must, consciously or unconsciously, build up. The point which has been emphasized is, that it is necessary to create good precedents consciously, so that they may be a sound basis for the future development of the financial system.

For this purpose it is obviously important that the members of the Indian Legislature should have the opportunities of studying the budget statements with some care. The budget statements are placed in the hands of the

members of the Legislature some time in the end of February, and the whole process of discussing the budget, voting the demands, considering and passing the taxation bills has to be finished before the 31st March, and this has to be done because the Central and the Provincial Governments must get the budget through the Legislature before the expiry of the financial year. Just six or seven days are allotted for voting the demands for grants. In these days scores of demands have to be voted upon, and hundreds of motions for amendments disposed of. Then the Finance Bill or the Taxation Bills have to be dealt with, amended, and passed. This means that the things have to be done in a hurry and disposed of in a way which makes the mature consideration of the points at issue practically impossible. It has already been said that it is necessary for the members to have a thorough grasp of the principles and details of financial policy of the Government before the budget session opens. The changes which the Executive proposes in a particular year can be understood without much difficulty if the present position is fully known. But even then the time allotted for the disposal of the budget is inadequate. In the United Kingdom twenty days are allotted for the consideration of the estimates. These days are not consecutive, and it is possible for the members to devote the intervening days for the detailed study of the estimates. But in spite of it, their detailed scrutiny is held to be unsatisfactory there. A committee for the detailed study of the estimates has been appointed to examine them in detail, but according to the view of a competent critic, the Estimates Committee has belied the hopes as an instrument of economy.[1] In India we have got the Finance Committees of the Legislatures. Their main function is to consider all the important proposals for new expenditure pertaining to votable items. It is not possible to say how far the committees have been able to do useful work; but from the time which the committees are known to spend in examining the new proposals, it would appear that their

[1] *Vide* E. Hilton Young, "The System of National Finance," p. 93.

examination could not be very thorough or searching. It is also the function of the Finance Committee of the Central Legislature to suggest economies in habitual expenditure, but that function has not been discharged by it. It is impossible for a committee which meets a few days before the session begins to examine thoroughly the estimates of even one department, and suggest economies therein. The problem is difficult. There are difficulties to be got over. It is necessary to keep intact the executive responsibility for the estimates. In India the Executive being irresponsible (leaving the ministers out of account) the consideration is not as weighty as in those countries in which the Executive stands or falls by the vote of the Legislature. It is, however, desirable not to undermine the executive responsibility for the estimates. On the other hand, it is essential to give the Legislatures opportunity of examining the estimates thoroughly, and effectively. The problem of the financial control of the Legislatures in India is different. It is not sufficient to scrutinize the proposals for fresh expenditure. The existing scale of expenditure needs looking into. A scale of expenditure has been set up here which, it is admitted by all, the country cannot afford, and its continuance is due to traditions which are foreign to the real nature of democracy. The standing committees of the Legislature cannot be expected to reduce the scale, which has been established by the practice of years. A Commission of National Expenditure, or a Commission of Economy and Efficiency, like the one which President Taft appointed in America,[1] will have to be appointed here to investigate the whole financial administration of the

[1] In 1911 President Taft appointed this committee for suggesting proposals for putting the finances of the United States of America on an economical and efficient basis. The committee was of opinion that one preliminary condition of carrying out any financial reform in America was the establishment of National Budget System. In India a committee with the same name and terms of reference will have to devote itself to the task of devising measures for reducing the expenditure in order that it may bear some reasonable proportion to the economic resources of the bulk of the taxpayers. Ever since 1804 when the Marquess of Wellesley, while ordering the building of the Government House, Calcutta, declared : " India should be governed from a palace and not from a counting-

country, and suggest measures for remedying this deep-rooted evil. That would not, however, dispense with the necessity of the vigilant control of the Indian Legislature. The experience of other countries is, it is true, a little disappointing. The pressure of public opinion, and popular Legislatures is in the direction of expenditure, rather than economy. Mr. Wattal in his book, "The Financial Administration of India," has given a few instances to show that the same tendencies have begun to work in India. But it has almost been an article of the national creed that the public expenditure is far too heavy for the capacity of the nation to bear it, and its reduction would be the first duty of the Indian Legislature, which really represented the Indian people, and had the power to give effect to their wishes. It may, therefore, be hoped that the Legislature in India would pay greater regard to the considerations of economy, and use their power to break the Mughal traditions of expenditure, which have so firmly established themselves in our financial administration. The first condition of doing this work is that the Legislatures should have sufficient time for going through the financial business of the year. The Finance Member said in reply to a question, in which the need for revising the procedure for placing the demands before the Assembly was suggested, "No question, I think, is more difficult than how to place before a parliament the estimates of expenditure of the year. I do not understand whether the Honourable Member in moving this (proposal) desires to complain of six days being insufficient as a whole, or of the general procedure. I think that the experience, so far I understand, of the last two years has not made it appear that the

house," the English in India have sought to surround themselves with buildings and other paraphernalia of the Government which can have no place in a democratic country. The whole administration is now saturated with traditions which make it necessary for the public servants to keep aloof from the people and strike their imagination by their aristocratic standard of living. All this has to be changed. It is extremely difficult to do so, as the evil is of indigenous growth, and our English rulers have merely adapted themselves to it. It is the mantle of the Mughals which has fallen on the English shoulders.

six days are really insufficient."[1] The figures of the demands which have been passed without discussion in the last four years point to the opposite conclusion. Six days coming one after another are evidently insufficient for dealing with sixty-five demands, when the object of motions for reduction is not merely to raise political discussions but also to bring home to the Executive the considerations of economy. The extension of the period during which the financial business has to be gone through is, therefore, necessary. This cannot be done if the present condition of finishing the financial business of the year before the 31st March remains in force. In the United Kingdom provisional authority is given by the Parliament to levy taxation and incur authorized expenditure till the consideration of the budget is completed, when the final authority for the continuance of annual taxes and the spending of money is granted.[2] In India the introduction of a similar procedure, though not extending over the same period, will make it unnecessary to rush through the voting of supplies and passage of taxation bills before the commencement of the next financial year. A detailed study of the budget estimates by the Legislatures is not possible under any circumstances. This can only be done by constituting the committees of the Legislatures consisting of men with financial experience and training. The present Finance Committees, on account of the limited time that they devote to the study of the estimates, and perhaps, their composition, are not a satisfactory means of achieving

[1] *Vide* Legislative Assembly Debates Report, Vol. III, pp. 3596–97.

[2] In the United Kingdom the estimates are introduced sometime in February and their consideration is finished towards the end of August. But as the money is granted to 31st March, the Parliament gives provisional authority to the Executive to spend money for those services which have already received the sanction of the Parliament, by passing what is called the "Vote of Account." Provisional Collection of Taxes Act of 1913 enables the Government to raise revenues, and it can therefore, without waiting for the final authority of the Parliament, which is granted by the passing of the Appropriation and the Consolidated Fund Act, obtain funds for carrying on the administration of the country. This gives time to the Parliament for a longer consideration of the budget than it otherwise could give.

this purpose. If the Indian Legislatures are to fulfil, in the financial spheres, the hopes that may well be cherished of them, they should have efficient organization for the legislative study of the estimates, and the opportunities for affecting the financial policy of the Government. At present not only their financial powers are circumscribed in several respects, but they are also handicapped in the exercise of their powers by the limitations of time and opportunities. The whole problem of the financial procedure of the Legislatures has to be approached with a view to make their control more real than it is at present.

CHAPTER V

RELATIONS OF CENTRAL AND PROVINCIAL FINANCE

THE estimates having been dealt with by the Legislatures, the next step in the financial proceedings of the year is to give effect to them. The revenue laws become operative, and the revenue has to be collected ; and the expenditure is incurred according to the programme accepted by the Executive and the Legislatures. But before we undertake the detailed study of the system of collecting and spending money, it is worth while to break the continuity of narrative, and understand the relation of the central and provincial revenues, which has attracted a great deal of public attention. The importance of placing it on a sound basis is recognized. The problem is not peculiar to India, for the relation of local and imperial finance has agitated the minds and abilities of the British statesmen, while in the Federal States there are three-fold complications of local State and federal fiscal adjustments. The problem with slight variations is everywhere analogous. The fiscal problem of the local bodies is considered in another chapter. The Reforms have, on account of its constitutional importance, thrown the problem of fiscal adjustment between the Provincial and Central Governments into bold relief, and created some complications of their own. There is no difference of opinion that a very large measure of independence of the provinces of outside control must be a *sine qua non* of the political progress of India. The provincial autonomy without financial autonomy can have no meaning, and the present financial arrangements are based on the recognition of this obvious fact. They have, however, caused great dissatisfaction, and a feeling that some of the

provinces have been favoured at the expense of others has given rise to acute inter-provincial jealousies and recriminations. It is held that some of the provinces are getting more than their due share of the national income, and others less, and that the Central Government does not leave enough to the provinces to enable them to find money for the important national needs of education, sanitation, and the development of industries, for which they are responsible. The matter has been subject of discussion in some of the Provincial Councils, and has been thrice brought up in the Central Legislature ; and on all these occasions the discussions have not been lacking in warmth or animation. It has been discussed in the press and on the platform, and it would be difficult to find any speech or article among the numerous speeches or the articles which have been written or delivered on the subject, in which the present arrangements have been defended. The general dissatisfaction has not been mitigated by the argument with which the Government has sought to justify their continuance—the argument that they cannot be changed so long as the state of the Indian finances remains what it is. Their revision appears evidently necessary, or at least the question needs fuller consideration than it received at the hands of the Financial Relations Committee, ordinarily knows as the Meston Committee, which in a period of less than seven weeks submitted its report, and laid the basis of the present settlement.[1] The question has got a history of its own, and to understand it, it is necessary to trace the evolution of the present position, and explain it with reference to its historical setting.

[1] The Meston Committee formally opened its enquiry on the 5th February, 1920, and submitted its report on the 31st March, 1920. During this interval it visited Allahabad, Patna, Calcutta, Rangoon, Madras, Bombay, and Lahore, received members of the general public or representatives of public bodies, held informal consultation with the Heads of the provinces, and discussed the subject of their enquiry with the officer-in-charge of the Finance Department of each province. It is not surprising that the Committee was congratulated for the expedition with which it completed its mission, and it is as little surprising that the Meston award has given rise to so much discontent and agitation.

The story of the way the Provincial Governments have attained their present financial position has often been told. It will be narrated here very briefly to bring out its salient features, and show why there is widespread dissatisfaction with the existing conditions. For this purpose it is not necessary to go farther back than 1861. Since 1833 the public finances were centralized in the hands of the Government of India. Under the constitutional arrangements of 1861 the control of the Central Government was not in any way relaxed. The revenues of India were treated as constituting one individual fund, and applied for purposes of the Government of India as a whole. The Government of India exercised sole control over the entire Indian revenues, and were alone liable for all the demands that could be made thereon. The Provincial Governments had to apply to the Government of India for the means wherewith to satisfy their local needs, and for their guidance, had no authoritative ruling as to the limit within which each department was to keep its total expenditure or expenditure on any one department. No additional expenditure, whatever its amount, could be incurred without obtaining the sanction of the Government of India. It is difficult to believe that the Provincial Governments could not even engage a peon on Rs.10 per mensum without the previous permission of the Government of India, but that was the extent to which the centralization was actually carried.[1] The Government of India in distributing the resources were handicapped by their want of knowledge of the local conditions, and had to apportion them as best as they could. The result from the point of view of the country as a whole was very unsatisfactory. There was no fixed or intelligible principle

[1] Sir John Strachey writes: "They (Provincial Governments) could carry out no improvement, great or small, for which the actual expenditure of money was required. If it became necessary to spend £20 on a road between the local markets, to rebuild a stable that had tumbled down, or entertain a servant on the wages of $10 a month, the matter had to be formally reported for the orders of the Government of India."—*Vide* Strachey's "India: Its Administration and Progress," p. 121.

on which the distribution of funds could be affected. The expenditure of the provinces was determined not by their resources or requirements, but the attention that their Governments succeeded in securing from the Central Government—viz. by the amount of the clamour that they made. To quote the words of Sir Richard Strachey, which have become classic in this connection, "the distribution of public income degenerated into something like a scramble in which the most violent had the advantage with very little attention to reason." But what is more important from our point of view is that in 1871, the year in which Lord Mayo made the beginning of the decentralization, the level of expenditure that had been reached in different provinces was taken as the basis of the new arrangements, and the inequalities, which existed at that time, were stereotyped. The provinces, which had a low level of expenditure, either because their administration was more economical, or because it could not have access to the central authorities, or because having been annexed later than other provinces had not reached the high level of administration which some of the older or more progressive provinces had, was penalized for its economy, lack of self-assertiveness, or what was worse, its backward condition. That was the beginning of the inequalities, which the later changes have, if anything, accentuated. The object of the reforms of Lord Mayo was to make the Provincial Governments responsible for their local finances, and obviate the necessity of annual grants by the Government of India of an assignment for each department of administration in each province. With this object in view they entrusted to each Provincial Government the responsibility for meeting, from a permanently fixed grant, the expenses of certain definite services such as police, jails, education, and medical services. An increase of expenditure was to be provided for by savings in the existing charges or the imposition of certain local taxes. The need of making petty references to the Government of India was avoided by giving to the Provincial Government

power, subject to certain conditions, to create appointments up to the individual limit of Rs.250 per mensem within the limits of the resources assigned to them. The experiment proved successful both from the financial and administrative standpoints, and in 1877 the process of giving wider financial powers to the provinces was carried farther by making them responsible for some other heads of expenditure, assigning to them the financial control of services connected with general administration, land revenue, excise, stamps and law and justice, and giving them the financial interest in the development of revenues collected in their territories by handing them over the revenues raised from law and justice, excise, stamps, licence duty (now income-tax). But the income derived from these sources was not sufficient for provincial needs, and was supplemented by fixed grants. In 1882 the system came in for revision again. The practice of making fixed grants was abandoned, and instead the provinces were granted the whole product of some sources of revenue, and a share of the product of others, including the land revenue. In this year was introduced the system of classifying the heads of revenue and expenditure as Imperial, Provincial, and Divided. The Imperial heads were those the income of which was wholly appropriated by the Government of India, or the expenditure on which was its liability. The Provincial heads were, similarly, the sole concern of the provinces, and the Government of India allowed them considerable discretion in their administration, subject to certain restrictions. But there were other heads of revenue and expenditure which were jointly Imperial and provincial, their income and outlay being shared in certain proportions between the two authorities. The bulk of provincial revenue was derived from the divided heads. The Government of India gave to the provinces the same financial powers in regard to the divided heads, which they enjoyed with reference to purely provincial heads. These settlements or the "Provincial Contracts," as they were called, were quinquennial

and were accordingly revised in 1887, 1892, and again in 1897. In these revisions the Government of India, on account of its predominant position, modified the arrangement to its own advantage, and left the provinces just enough income to meet their estimated expenditure, any surplus being taken over by the Government of India and added to its own resources. The result was the provinces, just before the expiry of the quinquennial period, increased their expenditure, depleted their balances, and assumed the appearance of financial stringency, which might or might not correspond to actual facts. Again there was put a premium on unnecessary or wasteful expenditure. The provinces that husbanded their resources or economized the expenditure knew that they would thereby be providing funds for the extravagances of other provinces or giving to the Government of India an excuse for an unfavourable settlement at the next revision. The inequalities, which were inherent in the settlement of 1871, were increased still further, and the arbitrary character of these settlements became more pronounced. The income which was assigned to the provinces had little relation to their resources or unsatisfied requirements, its amount depending entirely upon their actual expenditure. In 1904 the Government of India made an important change in their policy, and placed its financial relations with the provinces on a semi-permanent basis. The practice of resuming the surplus of the provinces was abandoned, and their share of public income definitely fixed. The arrangement of having the Imperial, provincial, and divided heads of revenue and expenditure was continued, but as it was not liable to alteration by the Government of India (except in case of grave Imperial necessity or in the event of experience proving that the funds assigned to a Provincial Government were inadequate for its normal requirements) the provinces could have a reasonable assurance of having a continuity of financial policy, or not being deprived of the fruits of their self-denial or judicious administration. The revenues assigned to the provinces, under the arrangement

of 1904 provided for its normal requirements. They were supplemented by annual grants, contemptuously styled as doles, by the provinces, for special purposes.[1] In spite of these improvements no attempt was made to redress the existing inequalities. The continuance of divided heads of revenue and expenditure remained a source of great irritation. The Government of India, on account of its vital interest both in provincial revenues and expenditure had to exercise a fairly close control over the provincial

[1] The general features of the settlement of 1904 have been thus summarized by the Decentralization Commission in their report:

"Generally speaking the effect of the settlement is as follows. The Government of India receives the whole revenue accruing from opium, salt, customs, mint, railways, posts and telegraphs, and tributes from Native States, while the Provincial Governments get all receipts from registration and from the spending departments which they manage such as police, education, law and justice, and medical. The receipts from land revenue, excise, stamps, income-tax, and forests are divided between the Imperial and the Provincial Governments generally in equal proportions. The receipts from large irrigation works are also generally shared—those of the minor irrigation works are wholly provincial, as are civil works receipts other than those pertaining to the Imperial buildings. The bulk of the provincial revenue is derived from the divided heads.

Expenditure in connection with the sources of revenue which are wholly Imperial is Imperial also, while subject to minor exceptions the Provincial Governments are responsible for the whole of expenditure incurred within the provinces in connection with the land revenue (which includes district administration) registration, law and justice, police, jails, education, medical, stationery, printing, and provincial civil works. Charges relating to stamps, excise, income-tax, and forests are equally divided, while the incidence of irrigation expenditure follows that of the receipts. The Provincial Governments are also responsible for such scientific departments and minor administrations which they administer and for political charges in connection with the Native States under their control. But the bulk of the expenditure in connection with the Political Department falls on the Government of India, as do all ecclesiastical charges.

The charges thrown on the Provincial Government by these settlements being generally in excess of the assigned revenues, the difference is made up, as formerly, by a fixed assignment under land revenue, but the present policy of the Government of India is to enable each province to derive the bulk of its revenue from the growing revenues.

Moreover, with these quasi-permanent settlements the Provincial Governments have all received considerable initial lump grants, principally with the object of enabling them to undertake works of public utility at an earlier date than would have been possible from their ordinary revenues. Further, the ordinary resources of the provinces have been largely supplemented of late years by special grants principally for the development of police reforms, agriculture, and education, and the Government of India have also made a special assignment to supplement the ordinary resources of the District Boards."—*Vide* Decentralization Commission Report, Vol. I, pp. 29–30.

budgets, which were submitted to the Provincial Councils after they had been approved by the Government of India. The restrictions on their power to create new appointments or incur new expenditure, though relaxed to a certain extent, practically remained intact. In 1907 a commission was appointed to recommend measures, by which the financial and administrative powers of the Provincial Governments and other subordinate public bodies could be expanded without impairing the strength or unity of administration. Mr. Gokhale, who had already recommended in his evidence before the Welby Commission the abolition of the divided heads, reiterated his views before this Commission, and again suggested that certain heads of revenue like land revenue, excise, and forests should be made over to the Provincial Governments, and they should make a fixed annual contribution to the Central Government to be determined after a careful consideration of certain factors.[1] Almost all Provincial Governments

[1] It is interesting to recall that much reviled system of the provincial contributions had in Mr. Gokhale a very strong advocate. He in his evidence before the Welby Commission approvingly quoted the following recommendations of Lord Dufferin's Finance Committee of 1885, generally known as the Elliot Committee after its chairman, Sir Charles Elliot:

"(1) That there be no divided departments, but those departments of receipt and expenditure which are now wholly or almost wholly Imperial or which may be found convenient to make Imperial should be set on one side for Imperial purposes, and that the receipts and expenditure of the provincialized departments should be entirely provincial.

(2) That whatever sum by which the Imperial expenditure exceeds the income from those sources, which are not provincialized, should be declared the first charge on the provincial revenues.

(3) The provincial surplus which arises from the excess of receipts over expenditure should be the fund from which in the first place all Imperial necessities should be met before any increase can take place in provincial expenditure.

(4) And as regards the future growth of revenue, it, as far as possible, should be equally divided between the provincial and Imperial, subject to the condition that if the Imperial exigencies require a larger share, the Imperial share should be increased."

This scheme, which it will be noticed is in many respects similar to the scheme now adopted under the Reforms would, Mr. Gokhale claimed, remove irritation, secure to the Provincial Governments half the share of the growing revenues, to the Imperial Government the normal growth of the imperialized items and also half that of the provincialized items, leave to it the power to take more in times of sore

complained against the excessive intervention of the Government of India in provincial matters, and asked for a substantial extension of financial powers. The commission, while recommending measures for removing some defects, declared themselves against any radical departure from the principles governing the financial relations of the provinces and the Central Government, or materially diminishing the control of the Government of India over the provincial budgets. They, however, held that with the grant of wider financial powers to the Provincial Councils, it would be desirable to give to the provinces more distinct

need, and also put a check on its spending propensities. He concluded his arguments with the following words:

"The adoption of this scheme will place the financial system of India once for all on a sound basis and will bring it more in line with the federal system of finance in other countries, such as Germany, Switzerland, Canada, and the United States of America."—*Vide* the Welby Commission Report, Vol. III, p. 218.

In his evidence before the Decentralization Commission Mr. Gokhale again advocated the system of the distinct provincial resources and provincial contributions. He said: "There should be no divided heads of either revenue or expenditure, but certain heads of revenue with expenditure under them should be wholly Imperial and others wholly provincial. I would thus assign to Provincial Governments independent sources of revenue in place of grants which they at present are understood to receive from the Government of India. The three major heads of revenue which I would make over to the Provincial Governments are land revenue, excise, and forests, which are intimately connected with the daily life of the masses of the people. On the other hand, the revenue and expenditure of opium, salt, customs, assessed taxes, stamps, registration, and tributes from the Native States, together with posts and telegraphs, mint, railways, and major irrigation works may be treated as wholly Imperial. On this basis of division, the revenues of all Provincial Governments will be found to exceed their present scale of expenditure, while the reverse will be the case with the Government of India. To make up this deficit of the Supreme Government, the Provincial Governments should make to it fixed annual contributions which should be determined after a careful consideration of the average liability of each province to famine, as also the need of making increased grants to local bodies out of the provincial revenues. Their contributions, moreover, should be liable to be revised every five or ten years, the revision taking place at a conference of the Revenue Members of different provinces presided over by the Finance Member of the Government of India. To meet sudden and extraordinary emergencies the Viceroy should have the power of altering the amount of these contributions as he may deem necessary, any Local Government feeling aggrieved by such alteration having the right of appeal to the Secretary of State."

It may be added that the Decentralization Commission was opposed to the system of provincial contributions.—*Vide* Decentralization Commission Report, Vol. I, pars. 65–68.

TABLE SHOWING THE FINANCIAL POSITION OF THE PROVINCES IN 1920–21

1	2	3	4	5	6	7	8	9	10	11	12	13
Provinces	Revenue collected *per capita*	Revenue contributed to C. G. *per capita*	Percentage of col. 2 to col. 3	Provincial Revenue *per capita*	Expenditure *per capita*	Expenditure on Genl. Admn. per 100	Expenditure on G. A. per sq. mile	Expenditure on education per 100	Expenditure on Law and Justice per 100	Expenditure on Police per 100	Expenditure on Police per sq. mile	Expenditure on Public Health per 100
	Rs.	Rs.		Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Madras	5.3	2.9	55%	2.4	2.7	7·6	20.17	32	35	41.6	132	16.7
Bombay	19.3	13.6	69%	5.85	6.53	25.6	39.8	74.5	57	90	143	30
Bengal	7.35	5.5	70.45%	1.85	1.97	8.15	50.5	23.4	36.1	35.2	218	10.8
U. P.	3.25	1.29	40%	1.96	2.22	7.6	31.9	26.5	28.8	37.1	166	8.55
Punjab	5.9	2.55	43%	3.35	3.7	13.4	27	36.1	44	47.8	96	15.8
Burma	17.8	5.7	31%	12.	6.7	23.1	12.9	35.5	58.1	140	78.5	26.3
Bihar and Orissa	1.48	.38	25.6%	1.1	1.32	5.6	27.6	15.9	23.4	20.4	83.5	5.6
C. P.	3.2	.76	23.7%	2.48	3.1	10.35	15	30.65	40.13	40.26	56	11.4
Assam	3.7	.49	16.3%	2.5	2.65	13.6	18.6	28	23	39.6	55.6	14.3

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sources of revenue, and concomitantly more final power over the budget. The recommendations of the commission were accepted. The provinces were given greater latitude in certain matters, but the main features of the settlement of 1904, which was made permanent in 1912,[1] remained practically unchanged till 1921, when the Reforms made financial readjustment necessary.

It is of some interest to have an idea of the accumulated inequalities of years of financial experimentations. India is a vast country and the diversity of conditions existing in different parts make the comparison of figures of revenue and expenditure of different provinces a little misleading; but the table attached is illustrative of the disparity of treatment which the provinces received at the hands of the Government of India. The total provincial expenditure per head varied from 1·32 per head in Bihar and Orissa to 6·7 per head in Burma, the expenditure on general administration from 5·6 per cent in Bihar and Orissa to Rs.25 per cent in Bombay. It is, however, necessary to bear in mind the fact that the expenditure on general administration depends upon a number of factors, besides population. Area of the province is one of those factors. Bengal, whose expenditure on general administration was third lowest, if we calculate it *per capita*, tops the list, if we take the area into account; and the expenditure in Burma for the same purpose, which was second highest, if we calculate it on population basis, is lowest among the provinces, when calculated on the basis of area. The same considerations, however, do not apply to the figures of expenditure on education. In this case average expenditure ranges from Rs.15·9 per cent in Bihar and Orissa to Rs.74.5 in Bombay. The climate, area, and physical features of the province have some bearing on

[1] In the despatch of 25th August, 1911, in which the Government of India outlined their policy of decentralization they said: "The only possible solution of the difficulty would be to give to the provinces a large measure of self-government, until India at best would consist of a number of administrations autonomous in all provincial affairs, with the Government of India above them and possessing power to interfere in case of mismanagement."

the expenditure on education, but, generally speaking, the criterion of equitable treatment would require, that it should bear some relation to the population of the province. If this test be accepted, the pre-Reforms expenditure on education cannot be said to be regulated on the principle of justice. The expenditure on sanitation and hospitals, again, depends, to a certain extent, on population, though the natural factors have got greater importance in this case than in education. Bihar and Orissa and Bombay once more represented the extremes, the former spending Rs.5·6 per cent and the latter Rs.30. The expenditure on the administration of justice and police show the same differential treatment between the different provinces, though it is not easy to lay down any conclusive test, according to which it should be regulated. When it is remembered that before the Reforms the Central Government exercised a substantial financial control over the provinces, and the whole revenue of India constituted one central purse, the strings of which were held by the Central Government, subject to the general control of the Secretary of State in Council, it will be realized that for the different scales of expenditure in different provinces, the Government of India was directly responsible. Taking everything into account, Bombay and Bihar and Orissa were the most and least favoured provinces respectively. It is difficult to base any conclusions on the amount of the revenue contributed by each province to the Government of India out of the total revenues collected in the province;[1] for Bengal and Bombay, the two provinces which contributed about 70 per cent of the total revenue collected in their territorial jurisdiction, were in reality the collecting centres, and the people of these provinces did not themselves pay the total amounts of the taxes collected in these areas. But even taking these two provinces, which contributed about

[1] The fact that a very large portion of customs, including the cotton excise duty, was collected in Bengal and Bombay does not mean that the total amount thus collected was paid by the people of these provinces. In their case, to use the words of the Joint Report, "the locale of the collection of these taxes is no index of their incidence."

the same ratio of their revenues and about the same amount to the Government of India,[1] we find striking differences between the amounts of revenue allotted to each, and the scales of expenditure set up there. To Bengal was assigned the income of Rs.1·85 per head, while Bombay got Rs.5·85. Bengal spent Rs.1·97 per head, and Bombay Rs.6·53. For education Bengal obtained Rs.23·4 per cent, while Bombay received Rs.74·5. For hospitals and sanitation, in spite of its notoriously unhealthy conditions, Bengal spent 10·8 per cent, the corresponding figure for Bombay being Rs.30. Madras surrendered 55 per cent of its revenues to the Central Government, but Madras also was, to a certain extent the collecting centre for other provinces. The revenue collected by other provinces may be taken to have been paid by the people of those provinces; the ratio of revenue contributed by each varied from 16·3 per cent by Assam to 45 per cent by the Punjab. It is not necessary to analyse these figures further. One has to read the columns of the table from top to bottom to realize the nature and extent of the inequalities which were, to use the words of the Joint Report, "masked by the divided heads." The task of carrying on the financial administration of India from one centre, and apportioning the revenues on some equitable basis was too much even for the administrative genius of the Anglo-Saxon race, and that it was undertaken at all, in spite of its obvious impossibility, is either another illustration of the lack of imagination, which is admittedly not a British quality, or shows the supreme faith of our rulers in their national quality of somehow muddling through and coming right in the end. Be it as it may, the financial position of the provinces prior to the introduction of the Reforms was highly unsatisfactory. During the war on account of the additional taxation the national revenues have been considerably increased, but a large portion of this increase was appropriated by the Government of India. The provinces were asked to keep a check on their expenditure in order that

[1] Each province contributed about 25 crores.

the Central Government might have sufficient resources for the discharge of their Imperial responsibilities. Some of the provinces carried out this injunction with greater fidelity than others. The Declaration of 1917 called for the reorientation of the whole policy. The objective set out in that famous announcement was "the progressive realization of responsible government in India as an integral part of the British Empire," and substantial steps in that direction were to be taken as soon as possible. A radical change of this description could not but have an important effect on the financial relations of the Provincial Governments and the Government of India.

The authors of the Joint Report made it a cardinal principle of their proposals that the provinces be given the largest measures of independence—legislative, administrative, and financial—of the Government of India. The provincial autonomy was to be established in India, and in the words of the Joint Report, "if the provincial autonomy is to mean anything real clearly the provinces must not be dependent on the Indian Government for the means of the provincial development." The provinces were to be self-reliant and the practice of financing large and costly schemes of development by doles from the Government of India was to cease. There was to be an administrative clean cut—viz. clear demarcation of spheres of administration between the Central and Provincial Governments—the Central Government retaining in its own hands the control of those subjects which were pre-eminently of national importance, and leaving the remaining ones to the Provincial Governments. The subjects like national defence, railways, customs were to be assigned to the Central Government, and other subjects like education, sanitation, civil and judicial administration, and the development of industries were to be in charge of the Provincial Governments. As a natural corollary of the administrative clean cut there was to be the financial clean cut as well. The central sources of revenue were to be completely separated from the provincial sources. The

divided heads of revenue and expenditure were to be abolished, and the financial control of the Central Government over the Provincial Governments considerably relaxed. The provinces were to be given limited powers of taxation and borrowing-powers which they did not possess at that time. The problem of distribution of resources was difficult. To the customs and salt-tax—the two main taxes which were already mainly central—were to be added income-tax, on account of the need for the uniformity of rate, and that of getting over the difficulty, which has been felt all the world over of localizing the incomes, and the revenue from non-judicial stamps to avoid, again the discrepancy of rates. The provinces were to add remaining divided sources of revenue, viz. land revenue, judicial stamps, excise, and irrigation—to the purely provincial sources. Land revenue and irrigation were to be assigned to the provinces on account of their intimate connection with the whole administration in rural areas, and excise and judicial stamps on account of the convenience of administration. If this basis of allocation of resources was to be accepted, the Central Government would be left without adequate funds to carry on the functions assigned to it, and the need of meeting the resultant all-India deficit had, therefore, to be faced. Here the inequalities, which were the legacy of the past, at once presented themselves, and it was difficult to devise some means of finding funds for the Central Government, which would be accepted as equitable by all the provinces. It was recognized that it would not be possible to smooth out the existing inequalities, which were disguised by the complicated financial arrangements, and, therefore, the authors of the Joint Report proposed to make up the deficit by levying a fixed contribution on the provinces to be assessed as a percentage of the difference between the gross provincial revenues and the gross provincial expenditure, both to be calculated on the basis of a new scheme for the division of resources and functions. Taking the figures of 1917–18 as the basis of calculation, it was considered that

if each province contributed 87 per cent of its gross surplus, deficit in the Indian Budget would be covered. The objection to the plan that it would lead to some provinces bearing a much heavier proportion of the cost of the Indian Government than others, and would therefore evoke hostile criticism from the provinces adversely affected by it, was answered by pointing to the fact that each province would gain something under the new arrangement, and the inequalities, which it would bring into prominence, were already there, and would not become more flagrant under the new scheme.

The Government of India in their despatch of the 5th March, 1919, accepted the principle of covering the Indian deficit by a fixed charge on the provincial revenues, and assessing it as an all-round ratio of the gross surplus. But they contended that an arrangement which disclosed the true position of the provinces in the past would not, on that account, justify the continuance of the inequalities in the future. They, therefore, suggested that the initial scale of contributions should be treated as provisional, and steps be taken to fix a standard scale, to be determined on some equitable basis. As the whole question, according to them, needed skilled investigation, they urged that a committee of experts be appointed to enquire into the matter and recommend the initial and the standard scales of contributions. The Joint Committee accepted and endorsed this suggestion, and the Secretary of State, accordingly, appointed the Financial Relations Committee, of which Lord Meston was the chairman, to advise on the contributions to be paid by the various provinces in the financial year 1921–22, and their modification thereafter with a view to their equitable distribution.

The Committee submitted its report on the points at issue. It calculated that the deficit to cover which the contributions were to be fixed, would amount to 983 lacs. The authors of the Joint Report had recommended that the contributions should be assessed as the flat ratio of the excesses of anticipated income of the provinces according

to the proposed arrangements over the normal expenditure of the provinces on services committed to their charge. The Committee was of opinion that the basis of assessment was open to question on account of the difficulty of calculating the normal expenditure of the provinces, and making allowance for the fact that while some provinces had strictly adhered to economy during the war, others had increased their expenditure more freely, and would therefore gain on account of having to pay reduced contributions if their scale of expenditure at that time was to be accepted as normal for the purpose of calculating contributions. The advantages of the basis of the Joint Report could, in their opinion, be secured by another method which was less exceptionable. Their recommendation was that the basis of assessment should be additional spending power,[1] which each province would obtain under the new arrangement. The increased spending power being the result of political reconstruction could very well be made a suitable basis of the initial contributions—as it was something in the nature of a windfall-bye-product of a constitutional change which had no reference to the financial inequalities of the past settlements. The Central Government would not, in levying the contributions on this basis, be raiding the hard-won surplus of the provinces or become thereby their pensioner. In doing so it was merely withholding a certain proportion of the increased resources which it was placing at their disposal. They made another important change as well, as far as the initial contributions were concerned. The authors of the Joint Report had recommended that the contributions should be levied at an even rate on all the provincial figures. But the Committee was of opinion that this

[1] For calculating the increased spending power the revenue of each province before the Reforms was to be deducted from the revenue which they were expected to receive under the new arrangements and a certain proportion of the difference was to be taken as the provincial contribution. For example, it was calculated that Madras would get 14·98 crores of revenue under the Reforms. This would give it an increased spending power of 5·76 crores. It was to contribute 60 per cent of this amount or 349 lacs, which would still leave it the balance of 228 lacs, which was to be utilized for meeting the additional charges thrown on the province on account of the administrative arrangements and any fresh expenditure that it may like to incur.

apparently equitable arrangement would cause hardship in certain cases on account of the existence of very great disparity in the financial strength of the provinces. It considered the case of each province on its own merits, and submitted its recommendation with regard to each province on the basis of such consideration. Bihar and Orissa was, in its proposals, exempted altogether from contribution on account of its poverty, inelasticity of resources, the urgent necessity of raising the standard of administration, and providing it with the essential requisites of a self-contained province. Burma was to pay 6½ per cent of the total deficit on account of the need of giving it "reasonable administrative conveniences," which it lacked. The Central Provinces and Assam were also considered deserving of special consideration, as they had a small margin at the best of times, and their need for development was great, and were, therefore, to contribute only 40 per cent of their additional revenue. The remaining five provinces were, in their scheme, to contribute 60 per cent of their additional spending power to the Central Exchequer. The United Provinces and Madras were going to receive vastly increased resources, the Punjab was also to gain a great deal, Bombay had already attained a scale of expenditure far above the Indian average, and could, therefore, afford to wait for further development, and Bengal in spite of having a low scale of expenditure and inelastic resources, had economic possibilities, which made it unnecessary for the committee to recommend any differential treatment in its case. The total deficit of 983 lacs was to be made up by contributions, which are set forth in the table given in the footnote.[1] The criticism that Madras,

[1]

Provinces.	Contributions (in lacs) Rs.
Madras	348
Bombay	56
Bengal	63
United Provinces	240
Punjab	175
Burma	64
Bihar and Orissa	Nil
Central Provinces	22
Assam	15

the United Provinces, and the Punjab would have to pay $35\frac{1}{2}$, $24\frac{1}{2}$, 18 per cent respectively of the total initial contribution was anticipated by the Committee, and met by pointing out that the contribution did not represent any new burden, and that the weight of contribution by the provinces was the best index of their gains[1] under the new financial scheme; and as the Government of India was advised to direct its financial policy towards the reduction of these contributions with reasonable rapidity, and their ultimate cessation, the eventual gains of these provinces would be much greater than the immediate ones. The amount paid by the provinces being a measure of their increased resources could not be made a subject of legitimate grievance. It was recommended that the initial contributions, being of arbitrary character, should be treated as a measure of transition, and modified in a way as to conform to an ideally equitable standard. The standard contribution was to be assessed on the basis of "the capacity to pay" of each province. It was, however, not easy to find out the paying capacity of provinces. The statistics of the relative wealth of the provinces not being available, the Committee had to rely upon the indirect proofs of their productive capacity for fixing the standard contributions. They laid down on the basis of general considerations, fixed ratio of the total deficit which each province could be called upon to contribute, the amount being proportionate to the economic resources, both actual

[1] Table showing gains of the provinces under the new arrangements:

Province.	Estimated increased spending power under the Reforms (in lacs)	Amount of contribution.	Net gain.
Madras	576	348	228
Bombay	93	56	37
Bengal	104	63	41
United Provinces	397	240	157
Punjab	289	173	114
Burma	246	64	182
Central Provinces	52	22	30
Assam	42	15	27

and potential,[1] of each province. The process of transition from the initial to the standard contributions was to be commenced in the second year of the new arrangements, and completed in six annual steps. In the 7th year of the Reforms each province was to contribute the standard ratio of the deficit.[2] The Committee held that its proposals provided for rectifying the inequalities of the past without creating any immediate financial disturbance. There is one other recommendation of the Committee, which deserves special mention. According to the plan outlined in the Joint Report the General Stamps was to be a central head of revenue, and this suggestion, as already stated, was based on the assumed need of having a uniformity of rates. The Committee recommended that it should be made a provincial head in all the provinces. Their reason for suggesting this change was that without it some of the

[1] Statement showing the per cent contribution to the deficit of the Government of India which in the opinion of Meston Committee each province ought to contribute on the basis of its paying capacity :

Province.	Per cent contribution.
Madras	17
Bombay	13
Bengal	19
United Provinces	18
Punjab	9
Burma	6½
Central Provinces	5
Assam	2½
Bihar and Orissa	10
	100

[2] The steps by which the standard contribution was to be reached are shown in the following table :

Province.	Initial contribution.	2nd year.	3rd year.	4th year.	5th year.	6th year.	7th year.
Madras	35½	32½	29½	26½	23	20	17
Bombay	5½	7	8	9½	10½	12	13
Bengal	6½	8½	10½	12½	15	17	19
United Provinces	24½	23½	22½	21	20	19	19
Punjab	18	16½	15	13½	12	10½	9
Burma	6½	6½	6½	6½	6½	6½	6½
Bihar and Orissa	Nil	2½	3	5	7½	8½	10
Central Provinces	2	2½	3	3½	4	4½	5
Assam	1½	1½	2	2	2	2	2½

poorer provinces would start with little or no surplus,[1] that it would facilitate the initial distribution of the central deficit, and further that as the general and judicial stamps were controlled by the same agency the retention of the former as the central head would mean the continuance of the "taint of the divided head," which, on the implied premise of the clean cut, was highly undesirable. The difference in rates did not, in their opinion, constitute a very great difficulty, and where uniformity was absolutely desirable, it could be secured by central legislation.

These recommendations met with a varied reception. The Government of India accepted them in their entirety. Each Provincial Government approved of those proposals, which were calculated to be beneficial for it, taking exception to others which affected it adversely. The Governments of Assam, the Central Provinces, Bihar and Orissa, Burma and the Punjab were, on the whole, favourably disposed towards them, though the Government of Bihar and Orissa lodged its emphatic protest against the proposal of requiring it to pay 10 per cent of the total deficit after seven years. The reasons, which it was contended justified the exemption of Bihar and Orissa from the initial contribution, were as valid against throwing on her the liability of bearing the heavy burden of 10 per cent of deficit after seven years. The Government of the United Provinces was against the differentiation between provinces, and recommended that the initial contributions should be rateably distributed, and considered 18 per cent as an

[1] The need of starting each province with a working surplus at the commencement of its career under the Reforms was emphasized by the Meston Committee in the following words:

"It will clear the ground to state at the outset a limiting consideration by which we feel ourselves bound. This is an obligation to leave each province with a working surplus—a surplus which we should prefer to calculate so far as possible with some relation to general financial position of the province, and more imminent claims upon its resources.

Looked at somewhat differently, the limit we have imposed on ourselves that in no case may a contribution be such as would make it necessary for the province to embark on new taxation *ad hoc* which to our mind would be an unthinkable sequel to a purely administrative rearrangement of abundant general resources."—*Vide* Meston Committee Report, para. 11.

unduly heavy ratio, which the province, on account of the admitted need of making up the arrears of administrative progress, and inelastic revenues, could not be reasonably called upon to bear. But the three Presidencies of Madras, Bombay, and Bengal were the most vehement in their condemnation of the Meston Report. The Madras Government was against the transfer of revenue from general stamps to the provinces, protested against being required to contribute $35\frac{1}{2}$ per cent of the total deficit, wanted that the gradations from the initial to the standard contributions should be more rapid, and the provision be made for the extinction of contributions in a definite and short term of years. Bombay and Bengal laid stress on the magnitude of their indirect contribution in the form of customs, salt, and income-tax, were opposed to the progressive enhancement of their contributions to the central exchequer and considered the whole arrangement unfair as far as they were concerned. The Government of Bombay claimed half share in the income-tax without which it saw no chance of the success of the Reforms "in the most advanced province of India." The claim had been referred to the Meston Committee for its opinion, but had been rejected by it on the strength of the arguments urged against it in the Joint Report, which, in its opinion, were conclusive. The Government of Bombay held that the objections against the proposals were not valid. It was prepared to let the Government of India determine the rate of the tax, provided that it is allowed to share half its proceeds. The Joint Committee accepted the recommendations of the Meston Committee with one or two important exceptions. The allocation or revenues suggested by it was approved with this difference that the provinces were given a share in the growth of revenue derived from income-tax so far as the growth may be attributable to an increase in the amount of income assessed.[1] The provincial contributions to be paid in the

[1] The share of the yield of each province of the yield of income tax is determined in the manner laid down in the Rule 15 of the Devolution Rules:
"(1) There shall be allocated to each Local Government a share in

year 1921–22 were fixed at the amounts laid down by the Meston Committee, but the proposals of modifying them in order to put them on a more equitable basis was not accepted. The Joint Committee was against the increase of initial contributions payable by any province, but

the income-tax collected under the Indian Income-tax Act, 1918, within its jurisdiction. The share so allocated shall be 3 pies on each rupee brought under assessment under the said Act in respect of which the income-tax has been collected.

(2) In consideration of this allocation each Local Government shall make to the Governor-General in Council a fixed annual assignment of a sum to be determined by the Governor-General in Council as the equivalent of the amount which would have accrued to the Local Government in the year 1920–21 (after deducting the provincial share of the cost of special income-tax establishments in that year), had the pie rate fixed under sub-rule (1) been applied in that year, due allowance being made for any abnormal delays in collection of the tax.

(3) The cost of special income-tax establishments employed within a province shall be borne by the Local Government and the Governor-General in Council in the proportions of 25 and 75 per cent, respectively."

The working of this complex rule has thus been explained by Mr. E. A. H. Blunt, the Financial Secretary of the United Provinces Government, in his Note on the Financial Administration under the Reforms:

"We will suppose—

(1) That the total collection in 1920–21 were 54 lacs;
(2) That there is only one income-tax rate of 9 pies;
(3) That the cost of special income-tax establishment was Rs.2,40,000 in 1920–21;
(4) That the total collections in 1921–22 were 60 lacs and the cost of establishment 3 lacs.

Then with total collections of 54 lacs at 9 pies in the rupee, the number of 'rupees brought under assessment in respect of which the income-tax has been collected' (Rule 15(2) read with Rule 15(1)) would be 1,152 lacs. The 3-pie rate applied to this figure would give 18 lacs. From this must be deducted 25 per cent of Rs.2,40,000 or Rs.60,000. The net amount would therefore be Rs.17,40,000: and this would be the 'fixed annual assignment' of Rule 15(2). In 1921–22, with total collections of 60 lacs, the total income assessed would be 1,280 lacs. The 3-pie rate applied to this would give 20 lacs and this would appear as the provincial revenue from income-tax under Rule 14(c), balanced by items on the expenditure side of Rs.17,40,000 fixed assignment, and Rs.7,50,000 being 25 per cent of the cost of establishment in 1921–22. The net gain to the province on these figures would be Rs.1,85,000."

This rule has since been revised and its working simplified. Now whenever the assessed income of any year of any province exceeds the assessed income of 1920–21, the Local Government of that province is credited with an amount calculated at three pies in each rupee of the amount of such excess. From 1922–23 entire expenditure on account of the collection of the income-tax is borne by the Central Government.

In 1922–23 the total yield of income-tax was 18·13 crores, out of which the provincial share was 14·53 lacs. That means that practically income-tax is a central head though inasmuch as its proceeds are shared by the Central Government with the provinces, it is not free from "the taint of the divided head."

recommended that if the improvement in the finances of the central Government permitted the reduction of the total contribution, the provinces which had to pay most should be the first to be benefited by any such reduction. The amount of contributions remitted was to be distributed between the provinces in the proportion in which their contributions exceeded a certain proportion of total contributions.[1] The Joint Committee emphasized the

[1] The amount by which the provincial contributions are to be reduced in any particular year is to be determined by the Rule 18 of the Devolution Rules, in which it is laid down that "when for any year the Governor-General in Council determines the total amount of contribution a smaller sum than payable for the preceding year, a reduction shall be made in the contributions of those Local Governments only whose last previous annual contribution exceeds the proportion specified below of the smaller sum so determined of the total contribution and reduction so made shall be in proportion of such excess:

Madras, 17–90th; Bombay, 13–90th; Bengal, 19–90th; United Provinces, 18–90th; Punjab, 9–90th; Burma, 6½–90th; Central Provinces, 5–90th; Assam, 2½–90th.

It will be observed that the standard ratio of the whole towards which the provincial contributions are to approximate not by raising the amounts paid by the provinces whose initial contributions are less than the standard, as suggested by the Meston Committee, but by reduction of the contribution of those which are paying more when the reduction of the total contribution is possible, are the same as those which were recommended by the Meston Committee with this difference that they are, for some reason, shown as ninetieths and not as percentages. They are given as percentages in the following table, for which acknowledgment is due again to Mr. E. A. H. Blunt of the United Provinces Finance Department.:

Province.	Initial contribution in lacs.	Proportion of whole.		Fair proportions of whole.	
		Per ninety	Per cent.	Per ninety.	Per cent.
Madras	348	31·86	35·40	17·00	18·89
Bombay	56	31·86	5·70	13·00	14·45
Bengal	63	5·77	6·41	19·00	21·12
United Provinces	240	21·98	24·41	18·00	20·00
Punjab	175	16·02	17·80	9·00	10·00
Burma	64	5·86	6·51	6·50	7·22
Central Provinces	22	2·02	2·24	5·00	5·55
Assam	15	1·36	1·53	2·50	2·77
Total	983	90·00	100·00	90·00	100·00

The working of this rule can be explained by citing an example given by Mr. Blunt in his book: "Let us suppose that the Central Govern-

disadvantages of a system of provincial contribution, and recommended their very early cessation. The Government of India was asked to shape its financial policy towards the reduction and the ultimate extinction of these contributions. They recognized the peculiar financial difficulties of the Presidency of Bengal, and commended its case to the special consideration of the Government of India. The financial scheme approved of by the Joint

ment reduces its deficit and consequently the total contribution by 173 lacs to 810 lacs. We then get rounded figures (in lacs) as follows:

Province.	Last previous contribution.	Fair proportion of new contribution.	Excess of last contribution.	New contribution.
Madras . . .	348	153	195	258
Bombay . . .	56	117	—	56
Bengal . . .	63	171	—	63
United Provinces .	240	162	78	204
Punjab . . .	175	81	94	131
Burma . . .	64	58·5	5·5	62
Central Provinces .	22	45	—	22
Assam . . .	15	22·5	—	15
Total . .	983	810	372·5	810

(The figures in the fourth column are obtained by subtracting the figures in the third from those in the second column. The figures in the last column are obtained, e.g. in the case of Madras, by the calculation $348 = \frac{195}{372\cdot5}$ of (983 = 810)).—*Vide* Blunt's "Note on Financial Administration under the Reform Scheme," p. 24.

In the Budget discussion of 1925 Sir Basil Blacket gave an idea of the way the rule would work. He said:

"The present 2½ crores remission reduced the Madras contribution by Rs.126 lacs; United Provinces, Rs.56 lacs; Punjab, Rs.33 lacs, and Burma, 9 lacs; the next Rs.1½ crores reduction would reduce Madras by Rs.59 lacs; the United Provinces, Rs.45 lacs; Punjab, Rs.30 lacs; Burma, Rs.14 lacs, and Assam, Rs.2 lacs. The next Rs.1½ crores remission would reduce Madras by Rs.43 lacs; Bombay by 15 lacs; Bengal, Rs.3 lacs; United Provinces, Rs.41 lacs; Punjab, Rs.23 lacs; Burma, Rs.14 lacs; Central Provinces, Rs.6 lacs, and Assam by Rs.5 lacs. A further remission of 1½ crores would reduce Madras by Rs.28 lacs; Bombay by Rs.22 lacs; Bengal by Rs.32 lacs; United Provinces by Rs.30 lacs; Punjab by Rs.15 lacs; Burma by Rs.10 lacs; Central Provinces by Rs.9 lacs, and Assam by Rs.4 lacs, leaving a balance which would be finally wiped out by the next reduction in case of Madras by Rs.25 lacs; Bombay by Rs.19 lacs; Bengal, Rs.28 lacs; United Provinces, Rs.27 lacs; Punjab, Rs.13 lacs; Burma, Rs.10 lacs; Central Provinces, Rs.7 lacs, and Assam, Rs.4 lacs."

Committee was incorporated in the Government of India Act.

The arrangements have been at work for about four years. The Government of India has not been able to reduce the provincial contribution on account of its unsatisfactory financial position.[1] The contribution of Bengal has been suspended for a period of three years, but the concession has been extended on account of special recommendation of the Joint Committee.[2] The Government has repeatedly declared its policy of reduction and eventual abolition of the provincial contributions. The reduction of the provincial contributions is to be the first charge on the betterment of the Indian revenues. But unfortunately the anticipations on which the Meston Committee based its calculations have proved wide of the mark. This discrepancy between actual facts and the assumed basis of the financial settlement is due to circumstances for which it is not easy to hold any one responsible. The provinces instead of having working surpluses, the possession of which was considered an essential condition of the success of the new arrangements, have had large deficits in the first three years of the Reforms. The Meston Committee spoke of the abundant general resources, which, as a matter of fact, have hardly proved adequate for carrying on the ordinary administration of the provinces. They considered it unthinkable that the provinces should embark on new taxation as a result of the administrative rearrangements, while almost all provinces have had to increase existing taxes or impose new ones to balance the budgets. The ministers, of whom a great deal was naturally expected, have found themselves handicapped by the want of funds. The Central Government has had financial difficulties, which the Meston Committee did not

[1] Since the above was written the total contributions have been reduced by 2½ crores, and the amount distributed among the four provinces in the manner indicated in the footnote on p. 163.

[2] The concession has been extended for another period of three years, and it is very unlikely that Bengal will be called upon to contribute anything to the central revenues so long as the present arrangements are continued.

(and probably could not) take into account. The Meston settlement was, as far as the Central Government was concerned, based on certain assumptions, which the events have falsified. It was taken for granted that the rate of exchange would be 2$ a rupee, while the actual rate has, for the last three years, been about 1s. 4d.—a circumstance which was bound to be a great disturbing factor in the Indian finances.[1] The military expenditure, which was taken at 42 crores rose to 67·75 crores, and now stands at 63 crores. The railways, which were expected to make a net contribution of 8 to 10 crores to Indian revenues have on account of the increase of the working expenses and the falling of the receipts, not even been able to pay their working expenses and the interest charges. The Government of India, in spite of heavy additional taxation, and considerable reduction expenditure, has just been able to balance its budget after three years of heroic struggle.[2] The situation, both of the central and provincial finances, has distinctly improved in 1924, but it is not reassuring as yet. The Central and Provincial Governments are still sailing very near the wind, the margin of revenue over expenditure being very narrow, and the funds for financing schemes of social and economic development practically non-existent. The situation is not as dismal as it is often represented, but is far from satisfactory.

The problem is admittedly very difficult. It is not

[1] The Government of India has to make payments in England in sterling—the English money. These payments are very large, the anticipated amount for 1923–24 being about £42 millions. The Indian revenue is collected in rupees and the payment in England has to be made in sterling. The outgoings of the Government therefore depend upon the rate of exchange between the rupee and sterling, the slight variation from the assumed rate making a difference of crores in public expenditure. The rate assumed for 1924–25 is 1$ 4d., but if the actual rate is 1$ 5d., the Government will if the present estimates of sterling remittances turn out correct, make a saving of 1·71 crores in its outgoings. The difference between the 2$-rate which the Meston Committee assumed and which is still the official rate, and the actual rate has, of course, increased the liabilities of the Government by many crores, and been partly responsible for the heavy deficit of 1921–22 and 1922–23. The total net loss in 1922–23 on this account amounted to 16·61 crores.

[2] In two years—1921–22 and 1922–23—the Government of India have raised revenue to the extent of 28 crores by additional taxation,

merely a question of provincial contributions. All are agreed that they are an evil and, from the standpoint of the Government of India, a necessary evil. The Government of India is pledged to their final abolition. Some relief could have been afforded this year to Madras, the United Provinces, and the Punjab, if the Legislative Assembly had agreed to the fixing of the salt tax at Rs.2 per maund.[1] There is a revival of our international trade, and the customs revenue is bound to increase. Railways are once more on their way to become a paying proposition. With the return of economic prosperity the income-tax receipts will also mount up. If there is no corresponding increase in the expenditure of the Central Government, the provinces can very well look forward to the reduction of contributions in the near future. The provinces are naturally feeling impatient at the delay, which has already occurred in the fulfilment of the promise. The Government of India have wisely abstained from giving any undertaking regarding the pace of the reduction of contributions or the period after which they are to cease. The world forces have been already too strong for them, but the policy, which has been enunciated so often, makes it certain that the cessation of the contributions is only a question of time, and it may be hoped, not of a long one. But the problem, from the point of view of the provinces, has another and a graver aspect. Land revenue has been called the sheet anchor of provincial finance. The figures will show that this description is well deserved. The other head of provincial revenue next in importance to the land revenue is excise.[2] The future of both the land revenue and excise is quite problematical. The receipts from these two heads do not show much buoyancy.[3] But what is of greater

[1] This was written in May, 1924.

[2] Out of the total provincial revenue of 75·73 crores, land revenue accounts for 34·92 crores, and excise for 13·03 crores. They, between themselves, were responsible for about 64 per cent of the total provincial revenues.

[3] This is practically true of the total provincial revenues taken together. The Accountant-General of the United Provinces has, in his Appropriation Report of 1921–22, given the following figures of the

importance is that the fiscal reforms of the future are very likely to make them less productive than they have been in the past. The enthusiasm of the politically-minded classes in India for the permanent settlement has abated since the time of R. C. Dutt, but still the pressure is in the direction of increasing the period of the settlements, lowering the maximum proportion of the net produce which can be taken by the State, and fixing the limit of individual enhancement, measures all of which will lead to the reduction of the yield and the land revenue. There are a number of financial theorists, who advocate the assimilation of land revenue to the income-tax—a reform which the considerations of equity make, in spite of its administrative difficulties, pre-eminently desirable. If this proposal is given effect to, two opposing tendencies will affect the revenue of the provinces. The introduction of the principles of graduation and differentiation[1] in the administration

gross yield of the provincial sources of revenue for the last five years, according to the new classification:

"1917–18=1147 lacs, 1918–19=1097 lacs, 1919–20=1266 lacs, 1920–21=1170 lacs, 1921–22=1264 lacs.

He draws pointed attention to the fact, which, as is evident, gives ground for serious apprehension. Taking the figures of net receipts of what now are the principal sources of provincial revenues—land revenue, excise, stamps, forests registration, and irrigation for all the provinces are as follows:

"1917–18=68·7 crores, 1918–19=71·5 crores, 1919–20=79·2 crores, 1920–21=78·6 crores, 1921–22=74·9 crores.

These figures are only approximately accurate, but roughly speaking they point to the same conclusion. The receipts from the provincial sources of revenue are not expanding, and if the development of the provinces is not to be absolutely arrested, some new sources of revenue have to be exploited.

[1] In almost all countries the elements of graduation and differentiation have been introduced in the tax systems. The principle of graduation or progression requires that the rate of the tax should increase progressively as the size of the income increases, and not proportionately. The principle of differentiation is based on the recognition of the fact that certain incomes increase on account of the social causes without any exertion on the part of the individuals concerned. These incomes are taxed at a higher rate than others as the presumption is that they are "unearned." The existing land-revenue system does not take the total income of the assessee into account in calculating the amount due from him. Land revenue is assessed on the basis of the total area of land brought under cultivation. A man who owns 5 acres or 5000 pays the same rate provided the land is equally fertile. And no distinction is made between "earned" and "unearned" income, though increase in

of the land revenue may result in the increase of the public income, while the exemption of the lower incomes will lead to its substantial decrease.[1] The net result will probably be the reduction in the amount which the land contributes to the public treasury. It is difficult to be dogmatic on a point the settlement of which depends upon so many cross currents of national life. But it can be safely stated that the land revenue cannot be counted upon to give the necessary elasticity to the provincial revenues. As regards the excise it is not necessary to say much. The British Government in India has often been charged with trading in the vice of the people for increasing its income. There is an amount of accumulated prejudice against this head of revenue. Prohibition has been declared as the ultimate goal of the Government policy in some provinces, though its immediate realization is held impossible. It may be that the zeal for temperance reform will be tempered by a lively sense of the realities of the provincial finance, when the Provincial Governments become wholly responsible to the Provincial Legislatures. But it is very doubtful whether the receipts from excise will grow to any appreciable extent. Some of the provinces have undeveloped resources which may, after some time, be expected to bring some grist to the provincial mills. Burma and the United Provinces have got forest wealth, which awaits exploitation. The rivers of the Punjab and its irrigation possibilities will make the revenues move there in the upward direction "with marked ease." Burma, Bihar and Orissa and the Central Provinces have got mineral wealth which, when worked up, will contribute to the economic prosperity,

productivity due to the investment of capital is made a ground for a favourable treatment of the assessee.

[1] In the assessment of income-tax in India all persons whose annual income is below Rs.2000 are exempted from the payment of the tax, the assumption being that their income constitutes what is called "minimum of subsistence," and they contribute their fair share of taxation in other ways. If land revenue is placed on income-tax basis, income below a certain amount will have to be exempted. As most of the agriculturists in India are very poor, it will lead to a material reduction of the income derived from land revenue. Col. Fagan, the late Financial Commissioner of the Punjab, is of opinion that the introduction of exemption will almost wipe off the receipts from land revenue.

and therefore the taxable capacity of these provinces. These potential sources of income will, however, involve initial outlay, and appear on the wrong side of the provincial balance sheet for some time to come. In some of the provinces the rates of taxation are lower than in others, and the process of levelling up can add to the resources of the provinces, in which there is room for raising the rates. Among the scheduled taxes there are some which have not been used, but even they do not hold any prospect of a considerable expansion of the provincial revenues. There are two among them, which, if imposed and properly administered, may bring not a negligible amount to the provincial exchequer. The one—the tax on what is called the unearned increment of land—is more suitable for the local bodies, the need of which is as great as that of the Provincial Governments, if not actually greater. The other—the tax on successions—presents some legal and administrative difficulties of its own, which make its use in the near future highly inexpedient. It is, therefore, easy to sympathize with the difficulties of the provinces which, faced by an insistent demand for expenditure on many beneficent purposes, do not know how to raise the necessary funds. Between the provinces themselves there is a disparity of resources, which makes an even progress of different parts of the country, about the need of which there can be no difference of opinion, exceedingly doubtful. Bombay with less than half the population of Bengal, the United Provinces, and Madras, has higher income than that of Bengal and the United Provinces, and just a little lower than that of Madras. As compared with Bihar and Orissa, which has got a population a little less than double the population of Bombay, the latter has three times the income of the former and a scale of expenditure, which not only the backward province of Bihar and Orissa, but also the other provinces of India will take years to attain. The annual income of Bengal, with its population of forty-six millions, the highest in India, is less than that of Madras, the United Provinces, Bombay and the Punjab, the last

two provinces having a population of only about twenty millions. The case of Bihar and Orissa has been referred to so often that it is not necessary to point out why it is not easy to take an optimistic view of its financial future. It is true that the financial difficulties of Bengal and Bihar and Orissa can be removed to a certain extent, if the Permanent Settlement is not maintained. It is difficult to say how far these provinces can increase their income by undoing the error of Lord Cornwallis, but that it will mean a substantial addition to their resources, there can be no doubt about. It is not known for how long the Permanent Settlement will be treated as sacrosanct, but so long as Bengal and Bihar and Orissa keep it intact, the other provinces of India can, with good reason, say that their financial difficulties are of their own making, and do not entitle them to any consideration, if they are not prepared to act with the courage required to rectify the mistake of the past. It is, however, an open secret that the Governments of Bengal and Bihar and Orissa have not got an unfettered discretion in dealing with the matter. The British Government in India, whose past is often represented as a record of a long series of broken promises, cannot, at a time of national ferment, afford to take a course, which whatever its soundness from the fiscal standpoint, can be interpreted as a breach of faith, and give another handle to the dissatisfied elements in the country to intensify the political discontent. The weighty character of these political considerations is evident, and the practical difficulties which they create in carrying out this measure of fiscal reform, make it impossible to look in that direction for the financial relief of these provinces. The National Governments at some future time may be able to face the consequences of unsettling this settled fact, and set things right for these provinces and the country at large, though even then the vested interest will put in a tough fight, and surrender their privileges after many a pitched battle. But an alien Government, whose difficulties are great and increasing, cannot be expected to raise another storm in

the interest of the abstract considerations of financial equity. It may, therefore, be assumed that the financial difficulties of these two provinces will retard their progress for some time to come. The United Provinces have got a large population, and limited resources. The agricultural block in power is using its influence to press upon the Government the need for reducing the fiscal burdens of the landed interests. With the remission of the contributions, this province, besides Punjab and Madras, will have smooth sailing for some time. The Punjab and Madras are comparatively well off, and will improve their financial position in the near future. Bombay has no just ground for complaint for the present, but its concern about the future, on account of its exclusion from the growing sources of revenue is justified, if the present settlement is treated as permanent. The Central Provinces and Assam have difficulties of their own. They are small provinces, and their means are anything but adequate for meeting the pressing needs of education and sanitation, and in the case of Assam of communications as well. The extinction of their contributions will not give them any relief, and their resources are not capable of any great expansion. One of the incidents of the economic position of the Central Provinces is their liability to famines, which makes their revenues very variable. Burma is the one province which is quite happy under the Meston Settlement. It is unnecessary to labour the point. The position is, in spite of overstatements about the unsatisfactory character of the Meston Settlement, very disquieting. For the time being the provincial contributions loom very large before the public eye, as they represent the anomalies of the present arrangements. But even when they have ceased, the problem of a sound fiscal adjustment between the provinces and the Government of India will remain and have to be solved.

It does not lie within the scope of this book to offer any solution of this highly intricate problem. The question requires a much fuller treatment than it is possible to

give in the limited space available here. A few words, however, may be said as to how it can be approached. It is a living issue and, therefore, does not, like all other issues of its kind, lend itself to the doctrinaire treatment. The canon of the clean cut, on which the present settlement is based, is sound as far as it goes, but it is possible to press it too far, and raise it to the dignity of a financial dogma, and apply it with unnecessary rigidity. The division of resources is needed for the demarcation of functions. India is a big country, and the mistake of governing it from one centre is not to be repeated on any account. Our political craftsmen have rightly made it a cardinal feature of their plan to accord to the provinces a large measure of independence of the outside control. The revival of divided heads is not to be thought of, if all that they stood for is to come in their train. The provinces must have a complete power over their budgets, and within the limits laid down by the national interests, liberty to adapt their administrative systems to their special requirements. It will take a long time to set free the forces of the provincial initiative and enterprise, which were paralysed by extreme centralization—a necessity forced upon India for maintaining the efficiency of the bureaucratic machine. It will, in view of these considerations, be a profound mistake to revert to any arrangement which may have the effect of sapping some of the incipient tendencies of free adjustment to the circumstances of a vast country with diverse conditions. But it would be a folly to make a red rag of the divided heads, and make it a means of rejecting all proposals of financial readjustment, which do not fall within the four corners of the existing arrangements. The provincial contribution are sometimes spoken of as the provincial "tribute," implying thereby as if it is essentially wrong for the constituent parts of a State to contribute money towards the maintenance of the National Government. The abolition of the present contributions is highly expedient, as it is almost impossible to find an equitable basis for their apportionment. But there is

nothing inherently unsound about the system itself. The recommendation of Mr. Gokhale regarding the levy of the contributions has already been referred to. The payment of the *matricular* contributions by the constituent States of the late German Empire to the Central Government was an essential feature of the German Federal Finance, and similar systems have not been unknown in the constitutions of other Federal States. The mere existence of provincial contributions is not incompatible with the largest measure of provincial autonomy. Nor is the provincial autonomy put in jeopardy by some or all the provinces sharing with the Government of India the receipts of some of the sources of revenue. The proposals for provincializing the income-tax have been rejected by the authors of the Joint Report, the Government of India, the Meston Committee, and Joint Select Committee, and arguments urged by all of them for taking that view are that it is necessary to have a uniformity of rates, and a broad tax jurisdiction to avoid the administrative difficulties arising out of the extended basis of the tax. The arguments are valid. The economic unity of India is proceeding apace. Incomes nowadays are, on account of the working of the forces over which we have no control, transcending provincial boundaries, and becoming national and, in a few cases, international in character. The difficulties are particularly grave in the case of the income derived from the Joint Stock Companies. If each province had its own income-tax, which it administered locally, there will arise complications of the same income being taxed a number of times. To quote Prof. Seligman, " One State may tax a corporation where it is legally domiciled, that is where its principal place of business is ; another State may tax the corporation where its property happens to be ; and the third State may tax the stockholder, where he chances to reside." The Tata Steel Works are located in Bihar, the company has got its head office at Bombay, and the stockholders reside in different parts of the country. Where and at what rate its income is to be taxed, if there are nine

provincial taxes with varying rates? The local income-taxes have not been a success in any country under the modern economic conditions. The objections against them are convincing. But an easy avenue of escape out of the difficulty is to let the Central Government levy, assess, administer, and collect the tax, and the provinces have a part or whole of its yield, if necessary. It has been contended that if the provinces are allowed to share the receipts of the income-tax, their autonomy will be endangered on account of the revival of the divided heads.[1] Income-tax is already in this sense a divided head. But apart from that fact, there is no danger involved to the fiscal or political autonomy of the provinces, merely because the Central Government fixes the rate of the tax, and ad-

[1] The Government of India in a despatch of theirs expressed their opposition to the idea of reverting to a system of divided heads in the following words:

"The abolition of divided heads was emphasized as the most important feature of the reform proposals in paragraphs 109 and 200–203 of the Montagu-Chelmsford Report, and was accepted as such without further discussion by all parties concerned. A clear division of revenues between the Central and Local Governments was the basis of the whole scheme of reforms and we consider it axiomatic that unless such a division is made, and entirely separate sources are secured to each Government, there can be no provincial autonomy in any sense of the term."—*Vide* the Government of India Despatch, No. 13, of 1922, dated the 13th July, 1922, par. 7.

Sir Malcolm Hailey, speaking on the question of the reallocation of the revenues, made the following remarks on the proposals that receipts from income-tax should be divided:

"The income-tax must be the same all over the country, and it has been universally agreed that the Legislature which lays down what those rates must be should also have the task of supervising the collection of income-tax and organization. What would be the effect, should a Local Government which gets half of income-tax demand that it should have the right to vary the local rate; and what becomes of provincial autonomy if it cannot do so? Do you eventually contemplate a state of things in which there are varying rates all over India and you have the adjustment of double incomes between the Provinces? If you are to give any real autonomy to the provincial legislature in regard to their sources of income, something like this must eventually happen."—*Vide* Legislative Assembly Reports, Vol. III, p. 561.

In India the provinces cannot be given fuller autonomy than what is enjoyed by the constituent parts of the United States of America, Canada, or Switzerland, and if it has been possible to have a system of the apportionment of taxes between the Federal Government and the State in those countries there is no reason why it should not be possible to introduce it here without unduly circumscribing the independence of the provinces.

ministers it, and the provinces take or share its proceeds. Prof. Seligman, who is an authority of international repute on matters relating to taxation, supports, in his well-known book "Income-Tax," his suggestion that the income-tax in the United States of America should be administered by the National Government under its direct supervision, and its yield distributed among the constituent States in the following words: "This is by no means a revolutionary suggestion as it may appear. It is found in some form or other in many countries, and not in a few American commonwealths. In England, for example, the income-tax is assessed by the Central Government and a part of the proceeds of what is known as the estate duty is allotted to the Local Governments. In France revenue from all leading direct taxes is apportioned between the States and the localities by the device of the *centimes additionals*, and the same principle is applied in part in Italy. In Germany the proceeds of certain indirect taxes are divided between the Federal and State Governments, and one of the important features in the recent budgetery scheme of the late Chancellor Von Bülow was a federally administered inheritance tax, a part of the revenue of which was to go to the States. . . . In Canada, it is well known the large part of the provincial revenues is derived from the proceeds of the taxes that are levied by the Federal Government." He concludes his argument by the general observation that "the principle of apportionment between the central and local authorities is hence one that is entirely familiar to the students of finance."[1] It is not suggested that the revenue from the

[1] Prof. Seligman has discussed the same question at length in the latest edition of his "Essays in Taxation." He points out that there are no less than five methods employed for regulating the fiscal relations of the Central and the Local Governments. They are:

"(1) The taxes are assessed by the local authorities with additions for the use of the Central Government.

(2) The tax is assessed by the central authority with additions for local purposes.

(3) Separation of the sources of revenue, partial or total, the partial separation being more common.

(4) The division of the yield, i.e. the revenues are collected by the central authorities but a portion of the yield is assigned to localities.

income-tax should go to the provinces, or Bombay or Bengal be allowed to take part of its yield. Bombay, which is most clamant in its demand for having a part of the receipts of the tax is, as already stated, fairly well off, and should not get any concession, unless the whole question of financial adjustment is taken up for revision, and its case is considered along with that of other provinces on its merits. But the trend of the argument developed above is that the apportionment of national taxes is quite in keeping with the requirements of complete provincial autonomy. The question of reallocation of resources will have to be taken up sooner or later, and the provinces will have to be assigned sources of revenue, with

(5) The system of the subvention payments from the central to the local or from the local to the central.

Prof. Seligman is of opinion that the first and the fifth methods are unsuitable; the first because it leads to the underassessment of local property and the fifth because either the Central Government has to depend upon the largesses of the constituent parts or the latter depend upon the former for their revenues. He commends the third for its flexibility and adaptation by each Government of its fiscal system to its fiscal needs, but goes on to say: "While these advantages are undoubted, we must be careful not to push it too far. If by separation of resources we mean the liberation of the State from locally assessed property tax there can be no valid objection against it. But if by separation of sources we mean absolute distinct sources of revenue for central and local purposes, with no possibility of State sharing some of its revenue with localities the project is by no means beyond criticism. Moreover, a complete separation of sources may sometimes introduce fiscal embarrassments. It may, for instance, happen that a particular source of revenue assigned to either the State or the Federal Government be more than adequate for its purposes, while the source assigned to the other jurisdiction may be inadequate. There is no convincing reason why one kind of revenue should not be made use of to make good the deficit of the other." The second method he does not take exception to, though he is against undue reliance upon it for local revenues on account of the risk of increasing the rate to such an extent as to interfere with its maximum productivity. The fourth method—i.e. the division of the yield—meets with his special approval, and he sketches a solution of the problem of fiscal relations in the U.S.A. based on the partial separation of resources with the division of the yield in case of certain taxes which it is necessary to have administered by the central authority, but a part of the proceeds of which are to be assigned to States to give them adequate funds. He concludes his chapter with the following closing remarks: "In other countries the practical solution of the question will no doubt be different, but it is safe to say that throughout the world the trend of adjustment in the Federal State and Local Governments will be found in line with the solution sketched above."—*Vide* Seligman's "Essays in Taxation," 9th ed., chap. xxi, pp. 660–78.

some capacity for expansion. The complete separation of resources—understanding it to mean the assignment of some heads of revenue to the Central Government and others to the Provincial Governments, entire yield of which is appropriated by the authority which administers them—has the merit of simplicity, and is to be preferred to any other arrangement, if it can adequately meet the needs of the case. But if this simple solution is found inadequate for getting over the difficulty, the less simple solution referred to above should not be rejected for the fancied reason of its militating against the autonomy of the provinces. The proposal, as Prof. Seligman puts it, is not revolutionary, and is based on a device which has been tried in many countries, and has not interfered with the autonomy of the component parts of the Federal States. The suggestion has also application to heads of revenue other than the income-tax. To give another instance, the tax on successions, which has not been levied by any province as yet, will, if and when used, also lead to the conflict of jurisdictions and give rise to the difficulties of multiple taxation. A man may die in one province, his legal residence may be in the second, and his property may be located in the third province. The difficulties are likely to become more pronounced as the connection between the different provinces become more intimate, and it may, therefore, become necessary to entrust a number of taxes to the Central Government to secure a satisfactory measure of efficiency in their assessment and collection. It will not do, on that account, to make all the taxes which have to be administered by the Central Government, central heads of revenue. What is needed is that the different units of the State should have adequate and assured resources for performing the functions for which they are constituted, and should be free from vexatious interference of the outside agencies. The arrangements which will be suitable for achieving this end may have to be made somewhat elaborate, but everything should not be sacrificed for securing a simple solution of a complex problem. It

would perhaps be wiser to frankly admit its complexity, and work out an arrangement which may square with its essential character. All the provinces except Bombay and Bengal are against the reintroduction of the divided heads. It is easy to understand the dread of provinces of anything that bears even the remotest resemblance to the scheme of finance, which killed all provincial initiative, and aimed at standardizing even the most vital activities, the distinctive qualities of which ought to be spontaneity and variety of expression. But it is not a sound policy to go to the other extreme, and refuse to entertain proposals which, whatever their merit, may have the apparent "taint of the divided head." The reconsideration of the Meston Settlement is inevitable; and when it is undertaken it would be pedantic to rule certain proposals out of court merely because they evoke in the minds of the provincial executive the phantoms of the days of excessive centralization. Neither the system of provincial contributions, nor that of apportionment of revenues is in itself absolutely unsound. The financial relations of the Central and Provincial Governments have to be placed on a just and suitable basis. The way to do it is to understand the problem in its entirety; study the fiscal arrangements of the Federal States which have had to deal with similar problems and find a solution suited to our own peculiar circumstances. That is to be our ultimate goal. The intermediate one, of course, is the speedy extinction of the provincial contributions. That can be done by controlling the central expenditure, while the central heads of revenues, on account of the restoration of normal economic conditions, are on the up grade; and, if possible, by reducing it.[1]

[1] A provisional scheme for the reallocation of revenues between the Central and the Provincial Governments is outlined in a paper read by the author in the Session of the all-India Economic Conference, held at Benares in January, 1925. The paper constitutes Appendix X of this book. The author expects to write shortly a book on the subject of Federal Finance, in which the problem of the readjustment of financial relations between the Central and the Provincial Governments will be discussed at greater length.

NOTE.—It is convenient to refer in this note to the arrangement for the relief of famine which is part of the financial scheme of the Reforms. The question has a history of its own which it is not necessary to detail here. It is enough to say that till 1878–79 there was no regular provision in the Indian budget for famine expenditure. In that year it was recognized that as famine was an ordinary incident of Indian administration, the expenditure for the relief of famine-stricken people should be provided for from current revenues; and it was decided to increase the annual revenues by 150 lacs and assign the amount for famine relief. The relief of famine was the first charge on the assignment, and any amount left over was first to be used for the construction of protective works and then for the reduction or avoidance of debt. Prior to 1907–8 the expenditure on famine relief was a provincial charge until the provincial resources were exhausted, when the burden was shifted to Central Revenues. In that year the famine relief was made a central liability and it was decided to call upon provincial resources when the expenditure was really heavy. For this purpose an assignment of 37½ lacs was made in favour of the provinces liable to famine and distributed among them in proportion to their comparative need. In 1917–18 this arrangement was discontinued and the liability for famine relief was divided between the Central and Provincial Governments—three-quarters being central and a quarter provincial. Under the Reforms famine relief is a provincial subject and has to be met out of provincial revenue. According to the Rule 29 of the Devolution Rules, each province has to establish and maintain out of provincial revenues a famine insurance fund which can be spent upon famine relief, protective irrigation works and loans to agriculturists. The unexpended balances are transferred to the fund which forms part of the all-India balances, and the Government of India pays interest on the amount transferred to this fund which is also credited to the fund. It has been provided that as soon as the fund amounts to six times the annual assign-

ment the further provision for the assignment is to be suspended. The annual assignments which the provinces have to make have been determined by the experience of their liability to famine in the past and are as follows :

	Rs.
Madras	6,61,000
Bombay	63,60,000
Bengal	2,00,000
United Provinces	39,60,000
Punjab	3,81,000
Burma	67,000
Bihar and Orissa	11,62,000
Central Provinces	47,26,000
Assam	10,000

If, in any particular year, any province exhausts the amount outstanding in this fund, it can, if necessary, borrow money from the Central Government for famine relief, which has to be repaid in instalments. (*Vide* Appendix II.)

CHAPTER VI

COLLECTION OF REVENUES

THE collection of revenues, historically the most important financial activity of the State, is still the one operation which touches the lives of all citizens and makes them keenly aware of the existence of the State. The visit of the Revenue Officer or, what is more common nowadays, the receipt of a written demand that a certain amount has to be contributed to the public revenues and must be paid before a specified date is the most efficacious way of making the ordinary citizen realize that he owes some obligations to the State and must discharge them well. The mien of the tax-gatherer has been, and is still, stern; and it has not been found possible even in the most advanced self-governing democracies to raise public revenues without the use of the coercive power of the State—a factor generally kept in the background in normal times, but one whose existence is essential for providing the Government with the wherewithal for carrying on the administration of the country. "Mere willingness to support public services," to quote from Taussig's "Principles of Economics," "does not grow apace with the conviction of the need of public service." That is so in all countries. In India the existence of the foreign rule and consequent perversion of the political conscience of the people makes taxation more onerous and makes it still more unlikely that the public spirit can be relied upon to any considerable extent for the realization of the dues of the State. The fact makes the need of efficient and strictly honest revenue-collecting agency all the more paramount and one that is, on that very account, difficult to satisfy. It is well-known that our revenue departments are, collectively, the weakest link of the financial chain. That is due to causes which are deep-seated in the facts of

our political life and cannot be cured merely by improvements in organization and procedure. But the organization of these departments is far from satisfactory, and material progress can be made if the administration of these services can be improved by introducing radical changes in their constitution and composition. It has been said that the readiness with which people pay the taxes is a very good measure of the development of civic sense amongst them. It would be too optimistic to expect that the mentality of the people of India, so far as the collection of the taxes is concerned, can undergo any appreciable change in the near future; but the work of educating the public to a higher sense of duty in this respect will be rendered distinctly easier if the revenue-collecting agencies can be depended upon for fulfilling their functions honestly and well. As it is, they have acquired a reputation which will retard progress in this direction. With the political evolution of the country, it is necessary that the Revenue Officers should inspire greater confidence as regards their efficiency and honesty in order that the collection of taxes may proceed with as little friction as it is possible to achieve under the present circumstances.

The public revenues of India are composed of many ingredients. It is not possible to give a detailed account of the collection of all kinds of revenues. A fiscal system in which the State derives its revenues from so many diverse sources as it does in India, cannot be described in the limited compass of one chapter of a small book. It is a very complex system, has grown in a very haphazard manner and no attempt has so far been made to harmonize its different parts or handle and develop it in its entirety.[1] There are the ordinary sources of revenue which exist in all countries—viz. the direct and indirect taxes. There

[1] It is a little unfortunate that the proposal of the Government of India for constituting a Taxation Committee has been turned down by Legislative Assembly on the ground that an enquiry of that description should be preceded by an enquiry into the economic conditions of the people. The reasons which were urged in the course of the debate for rejecting the Taxation Committee show a misapprehension of the whole question. The necessity for an enquiry into the system of taxation in

are the State monopolies like salt and opium which yield large revenue and the proceeds of which are made up of both profits and tax-income. There are the great commercial departments of Railways and Posts and Telegraphs, which cannot be managed like other administrative departments of the State and have to be run on business lines, though the consideration of public utility can never be lost sight of in their management. There is, then, the land revenue, which as it has already been pointed out in the preceding chapters, has a position of its own in our fiscal system. It is an impost which it is not easy to characterize, but its collection has brought an elaborate machinery into existence which brings the public authorities in contact with the masses and makes the rural problem in India more intricate on account of the interest of the State in the systems of land tenure. It has its roots stretching back into the dim and distant past and is interwoven with the whole agricultural economy of the country. On account of the variety of the sources from which the public revenues are drawn, and the vast extent of the country over which they are collected, it is not, therefore, possible to go into details. All that can be attempted is to take two or three important sources of the central revenues, and as many of the provincial, and give a brief account of the way they are operated. Of the commercial departments nothing need be said in this connection. The methods of the collection of the revenues derived from them are a matter of common knowledge and do not call for any explanation. Of the central heads of revenues the most important are customs and income-tax. The latter may be taken first on account of the important changes that have

the country, in order to find out how far it is equitable and suitable, and in what direction it has to be changed for having a more scientific system, is immediate, and it is possible to separate the two questions of economic and taxation enquiry. The enquiry into the system of Indian taxation is long overdue. A Finance Member was right when he said: "As a matter of fact we are late in the day in making this enquiry."

Since the above was written the Taxation Committee has been appointed by the Government in spite of the adverse vote of the Legislative Assembly, and its report will most likely be available for the public before the end of 1925.

recently been introduced in its system of assessment and collection. The collection of income-tax is governed by the Income-tax Act of 1922. The most important feature of the Act is that it creates a new agency for the collection of the tax. Before the passing of this measure this work was done by the ordinary revenue staff—i.e. the Collector and his assistants. In the pre-war years it was comparatively simple, as there were only rates and all incomes above Rs.2000 were taxed at a flat rate of 5 pies in the rupee. During the war it became more complex on account of the introduction of a sliding scale of taxation, and the collecting agency, which even in pre-war years had been found wanting in a number of ways, was unequal to the additional work thrown on it. It was well-known that a considerable amount of income liable to the tax escaped assessment. The Act of 1922 has sought to remedy the defect. The graduated scale of taxation and the imposition of "an additional duty of the income-tax"—viz. the super-tax—have now become permanent features of the income-tax administration, and a special agency has, therefore, been created for its assessment and collection. In every province there is one Commissioner of Income-tax, who is appointed by the Governor-General in Council after consultation with the Provincial Government. He has under him an Assistant Commissioner of Income-tax, who helps him in the work of supervision, and several Income-tax Officers, who have to do the actual work of the assessment and recovery of the tax. The assessment is made by requiring the persons and corporations liable to the tax, to submit a verified return of their total income. It is the total income of the recipient from all sources to which the Act applies which determines the liability to income-tax and the rate at which it is paid. The Act confines itself to the definition of methods and procedure. The rates of income-tax and super-tax are laid down in the Finance Act of the year. The principal officers of the companies have, before the 15th June each year, to prepare and furnish to the Income-tax Officer a return, in the prescribed form, of

the total income of the company. In the case of other individuals, the Income-tax Officer serves a notice upon them requiring them to furnish a return of their total income within thirty days. If the Income-tax Officer is satisfied that the return furnished by the assessee is correct and complete, he assesses his total income on its basis and determines the sum payable by him. But if he has reasons to believe that the return submitted by an assessee is incomplete or incorrect, he can call upon the person concerned to produce his accounts and such further evidence as he may require to establish its correctness. On the basis of the evidence produced by the assessee, he has to assess his total income and determine the sum due from him. The next step is to recover the amount. The assessee has the right of appeal against the decision of the Income-tax Officer to the Assistant Commissioner, and if he is not satisfied with the order passed by him, to the Commissioner himself, whose judgment is final, save when the point of law is involved in which case the assessee can require that a reference be made to the High Court. But the fact that an appeal has to be lodged against the assessment cannot stop the collection of the tax, though, in certain cases, the Income-tax Officer has the discretion to let the demand or a part thereof to remain in abeyance till the appeal has been disposed of. As early as possible after the assessment, a notice is issued to the person concerned by the Income-tax Officer to pay the amount due before a specified date, and if he fails to comply with the order he invites upon himself the ire of the law and suffers the penalties which have been prescribed therein. The recipients of the salaries and interest on securities have, however, to submit, before they receive payment, to the deduction of a part of their income in advance. The deduction is made at the rate applicable to the estimated income of the assessee and treated as a payment of income-tax subject to subsequent adjustment when final assessment is made and recovery effected. This is the familiar method of what is called "the stoppage at the source." It is worth while to make it clear that this

deduction is not taxation at the source but only the deduction of the tax at the source. If, at the end of the year, it is found that more tax has been recovered than is really due, then a refund of the amount paid in excess can be claimed. If, on the other hand, it appears from the return of the total income that the assessee is liable to be taxed at a higher rate, an additional charge is raised against him and the sum already deducted at the source is set-off against the sum payable by him and the difference realized, in the ordinary way. The deduction from the interest of the securities and profits of the companies is made, in the first instance, at the maximum rate and the assessees are entitled to get refund if the maximum rate is higher than the rate applicable to their total income. By this method a considerable amount of the tax is collected in advance and the difficulties arising out of the concealment of income and similar other devices easily avoided.

The new Act has been in operation only for two years. There is no work more thankless than that of the Income-tax Officer. He has to steer clear of the two extremes of becoming inquisitorial on one hand and unduly lenient on the other. The work of assessment is highly technical and requires expert knowledge, experience, and a firm and tactful handling of men in order that, to use a somewhat inapt but expressive metaphor, the goose may be plucked with as little squealing as possible. It also exposes the officers to temptations that call for the use of a resisting power which only a moral fibre of very high degree can give. Income-tax must, in due course, become a powerful engine of finance in India, and whether its administration will give satisfaction and be relied upon for giving to our fiscal system the necessary quality of elasticity will depend upon the way the new organization is developed and manned. It must be realized that the assessment and collection of the tax require the services of efficient and honest officers, who are well-equipped for their work by their training and understanding of the complex economic relations and what is perhaps the most important, the

capacity to discharge their duties without any fear or favour. The ubiquitous civilians may be placed in charge of the administration, since no better qualified officers are available for the time being, but must, after some time, make room for officers who have a better title to the office than the possession of certain general qualities, however, excellent, which we are told will do for any job.

The Customs has, since the war, become the most important source of revenue in India. The Customs Department is administered by the Imperial Customs Service responsible to the Government of India. In each of the five principal ports of India there is a Collector of Customs who is also in charge of the minor ports under his jurisdiction. His staff consists, besides the clerical establishment, of Appraisers and Preventive Officers. On importation into or exportation from any port of any goods, the owner has to state the real value, quantity, and description of such goods and, of course, subscribe the declaration of the truth of such statement. The Customs Collector, like the Income-tax Officer, can require the owner, when he is not satisfied with his valuation, to furnish invoice, brokers' notes, policy of insurance, or any other document whereby the real value of the goods can be ascertained. The goods are then examined by an officer of Customs, and if it appears that real value has been correctly stated by the owner, the goods are assessed in accordance with it. If, however, the goods appear to be chargeable at a higher rate than that which the owner is prepared to accept, they can be retained for the use of the Government on the payment of the full amount stated by the owner and the goods disposed of to the highest bidder and the proceeds credited to the public Treasury. When the valuation fixed by officer of Customs is accepted by the owner, the duty leviable on the goods is assessed, and he is then given the option of clearing them for consumption on payment of the duty or deposit them in the warehouses which are appointed or licensed by the Government. When the latter course is adopted, duty and the warehouse

dues have to be paid before the goods are removed for home-consumption. The dutiable goods intended for export are similarly examined, appraised, and the duty assessed and paid before their shipment is allowed.

The work of tariff valuations will grow in difficulty as the protective movement gains momentum and the tariff schedules become more elaborate on that account. As the rates are raised, the possibility of evasion and the need for proper assessment of the goods will both become much greater. The administration of tariffs and its limitations have always to be borne in mind as the duties are enhanced in response to the demand for higher protection of indigenous industries. Till very recently we had what is called revenue-tariff, that is the Customs duties were imposed for raising revenue for the State. Now that the country is committed to the policy of discriminate protection, it has to be realized that the success of the policy will, to some extent, depend upon the ability and trustworthiness of the officers who are to give effect to it. This consideration suggests the necessity of paying a more close attention to the question of the tariff administration than they have hitherto received.

The two other sources of central revenues which deserve a passing mention are salt and opium. Salt revenue is derived from three principal sources—(*a*) Excise duty on Indian salt, (*b*) Customs duty on imported salt, (c) Sale of Government salt. About half of the indigenous salt is manufactured or mined by Government agency and half under licence on which the excise duty is paid. The imports usually represent about one-third of the annual consumption. The administrative system for the control of production and the collection of revenue varies with local conditions and methods of production. The duty on imported salt is collected by the Customs authorities. Opium is produced under Government supervision in the United Provinces and some of the Central India States and bought in its crude condition from the cultivators by the Government. It is manufactured at the Government

factory at Ghazipur, sold by public auction for export outside India and, in certain cases, direct to the Foreign Governments and issued to the Excise Department for local consumption for sale to the licensed vendors.

The administration of Customs, income-tax, salt, opium, and other minor heads of central revenue is under the control of the newly-constructed Central Board of Revenue. It has been created to centralize the administration of the various revenue departments of the Government of India. The powers and duties so far assigned to the Provincial Governments in respect of these heads have been transferred to this Board. The Inchcape Committee recommended[1] the constitution of this department in the interest of economy. But there is a more important reason which justifies its creation. In the United Kingdom there are two boards which manage and control the collection of taxes throughout the Kingdom and their chairmen are in constant communication with the Chancellor of the Exchequer, who is the responsible head of revenue administration. The Finance Member in India has, on account of the size of the country, no opportunity of having access to the sources of information which are within the easy reach of the British Chancellor of the Exchequer. The intercourse of the latter with the expert officers enables him to learn the defects in revenue laws or in the administration of the revenue departments and exercise his authority as the Chief Officer of the Revenue directly and effectively. With the delimitation under the Reforms of the respective spheres of the Central and Provincial Governments, the concentration of authority in the hands of administrative body in the close touch with the Finance Department of the Government will make it possible for the Finance Member to establish closer contact with the revenue administration and discharge his powers with regard to it more effectively. Though it is neither desirable nor possible to bring about the amount of centralization in revenue administration in India, which exists in the United Kingdom, the existence of a central supervising authority for controlling the

[1] *Vide* Inchcape Committee Report, Part IV, para. 19.

management and collection of the central revenues will be helpful for the Finance Member in following closely the fluctuations in receipts, ascertaining the causes of fluctuations and forecasting the progress of receipts. It is a step in the right direction and, as pointed out a little later, it is advisable to constitute boards with similar powers in the province to manage their revenue administration.

The Land Revenue and its administration are a matter of immediate interest to the great majority of population in India, and apart from their financial aspects, are of great importance from political and social points of view, and the most important branch of administration in every province is that connected with the assessment and collection of land revenue. There are great differences between the various provinces and often between different parts of the same province in matters of land revenue administration, and it is difficult to make any general statement with regard to it which is not subject to numerous exceptions. The variety and intricacy which characterize the revenue work make it difficult to indicate clearly, in brief space, even the principles and methods which underlie the various systems in force in the country. The revenue is levied by means of a cash demand in each unit assessed. In the provinces of Bengal, Bihar and Orissa, and some districts of the United Provinces, the demand is fixed in perpetuity and all that the Government has to do is to collect the revenue at specified intervals in instalments. In other provinces land revenue demand is fixed for a certain number of years, generally thirty, but is subject to revision after the expiry of that period. Before the demand is fixed for the period in question, land revenue "settlement" has to take place, which covers two distinct processes. The first is the preparation of the records of rights—ordinarily known as the cadastral records. A separate map is prepared for each village, the primary object of which is to show from whom the assessment of each holding is to be realized. These entries are, however, supplemented by additional entries in order to show the existing rights in the land for

regulating the relation of the occupants and proprietors of land. The second step of settlement is the assessment. For this purpose it is necessary to ascertain the "net produce" or "net assets"—terms which have different meanings in different parts of India. In Northern India and in the Central Provinces it represents rent or the portion of the gross produce which would have been taken by the landlord if the land had been let. In Madras and Lower Burma the net produce means the difference between the assumed value of gross produce and the estimated expenditure incurred by the cultivator, with whom the Government deals directly, for raising and disposing the crops. In Bombay, assessments are based on "general considerations" of the quality of land, economic conditions of the district, prevailing prices and other facts which have bearing on the income of the cultivators. The State takes a certain proportion of the net assets as land revenue. This standard is not determined by any hard or fast rule, but does not exceed 50 per cent of the estimated assets. In the application of the standard rates the assessing officers enjoy considerable latitude for exercising their discretion and can give free play to local considerations. The land revenue is generally collected in instalments, the dates and amounts of which are fixed to meet local circumstances. For the recovery of the amounts not paid by due dates the Government has extensive powers. A writ of demand and threat of attachment is sufficient for realizing the arrears, and in extreme cases the more serious process of the sale of land is also resorted to. For land revenue administration the district is the unit and the work is carried on under the general supervision of the District Officer. He has a staff of subordinates who do the actual work of assessment and collection. The low-paid functionaries who represent the Land Revenue Department in the villages are, as is very well-known, petty tyrants whose evil practices it is very difficult to detect and suppress but of the existence of which every one, who knows anything about the villages in India, is generally aware. The hardships which are

associated with the land revenue administration, are due as much to the incorrigible ways of these public servants as to the defects of the principles and methods of assessment on which the system rests. The revision of the whole system and its underlying principles is inevitable, and when it is undertaken the matter pertaining to its administration will need as much attention as the questions of the period of settlement, pitch of individual enhancement and standard proportion to be taken by the State as land revenue, on which, till now, the public discussions of the system have been focussed.

The other important source of the provincial revenue is, of course, excise. This term, in the Government accounts, deals mainly with taxation imposed on drugs and intoxicants produced in the country. The excise revenue is derived from these sources, duties on the issue of liquor and sums paid in respect of the right of retail sale. The normal excise system for spirits is based on the grant by contract of the right of wholesale supply and the sale by auction of the right of retail vend. Spirits are generally produced in central distilleries in which their manufacture and storage are under Government supervision, and the liquor pays duty before issue. The right of retail selling is sold annually or at intervals of not more than three years. It is held the advantage of this system is that it prevents the growth of vested interests, and that while it secures to the Government the highest revenue with least possible consumption, it enables it to keep the liquor trade under control. The systems of excise administration are complicated and vary greatly in different parts of India.

The two other sources of revenue in the provinces are Stamps and Registration. The stamp revenue is derived from two classes of stamps: judicial, or court fee stamps, affixed on all documents, with specified exception, filed before civil, criminal, or revenue courts, and non-judicial, or revenue stamps used for all commercial transactions recorded in writing. The revenue credited under the head "Registration" is derived from the registration of docu-

ments. Registration is compulsory in certain cases and optional in others. The administration of this department in each province is under the control of the Inspector-General, who has a staff of registrars and sub-registrars. The district officer is generally registrar ex officio.

Irrigation and forests are commercial assets of the Provincial Governments of great importance. Irrigation receipts are made up of water rates or the sale proceeds of water for irrigation purposes, land revenue due to irrigation and certain other miscellaneous receipts. Water rate and land revenue due to irrigation are collected by the Land Revenue Department. The principal source of forest revenue is the sale of timber and other produce of Government forests.

In all provinces there are either Boards of Revenue or Financial Commissioners. They, besides being a court of appeal in regard to the decision of commissioners, collectors, and other officers in revenue matters, perform important functions with regard to land revenue administration and, in some cases, that of the other sources of revenues as well. We have it on the authority of the Decentralization Commission that the original intention was to confer wide powers on these bodies to constitute them as general guardians of the fiscal interests of the State.[1] But as at present constituted they are held to be more or less superfluous, and particularly in the provinces in which there are divisional commissioners, their existence is considered unnecessary inasmuch as it is supposed that it leads to the reduplication of work. This view is put forward by some of the most well-informed critics of the Government finances and is weighty as far as it goes. But there is one consideration, which is of some importance in this connection. As Sir David Barbour pointed out in his evidence before the Decentralization Commission, our provinces are big enough to have independent financial systems of their own. The ideal of provincial autonomy assumes that each province will, in due course, have a self-contained financial

[1] *Vide* Decentralization Commission Report, para. 264.

organization, and for that it will be necessary to have a chief controlling revenue authority, which will be mainly concerned with matters of broad policy and help the Finance Member in the discharge of his duties in revenue matters. The considerations which have been urged in favour of the creation of the Central Board of Revenue are equally valid for the constitution of similar bodies in the provinces. The Decentralization Commission, while expressing themselves in favour of the retention of the Boards of Revenue in the provinces, were of opinion that they should be placed in the position originally intended for them—that of exercising wide authority in regard to revenue matters.[1] The Boards of Revenue with their present functions and powers may have to be abolished; but it will perhaps be more desirable to reconstitute them on a different basis and make them responsible for the entire revenue and not only land revenue administration of the provinces. It should be a deliberative and supervising body on which the officers in charge of the various revenue departments should be represented, who should give their collective opinion on all important questions connected with the revenue administration and revenue proposals, which will naturally carry greater weight with the public and the Government than the individual pronouncement of a single officer. The revenue administration requires expert handling and does not afford any scope for amateur financiering.

The revenues collected by the various departments—central and provincial—has to be deposited in the treasuries or the Imperial Bank as the case may be, the appropriation of departmental receipts for departmental expenditure being strictly forbidden. There are some minor exceptions to this rule which, however, do not effect its validity.

[1] *Vide* Decentralization Commission Report, para. 471.

CHAPTER VII

ESTIMATES IN OPERATION

THIS chapter and the next deal with the system of disbursement of public funds to the creditors of the State. The disbursement of funds involves three classes of activities. The initial step is the incurring of obligations. When the budget provisions become operative, it is the duty of the administrative officers to give effect to the financial policy of the Government by incurring the necessary obligations. The public liabilities are of different kinds. The officers of all grades have to be recruited, stores have to be purchased, contracts given and other activities, which throw charges on public expenditure, undertaken. Each officer, within the limits of his authority, issues the necessary orders. He has, before incurring the liability, to make sure that funds have been provided for the purpose, and charges sanctioned by a competent authority. The extent to which the charges are incurred, with due regard to the considerations of economy and efficiency, depends upon the integrity and ability of the officers concerned. The next step, after the obligation has been incurred, is to liquidate them, or determine their value. The permanently sanctioned establishments have their bills prepared by the accountants, which are signed by the responsible officers, and the amounts necessary for making payments drawn from the Treasury. But there are certain public charges, which require careful scrutiny before they are passed for payment. The fluctuating charges on account of the travelling allowances and contingencies, and the claims of the people not in Government service have to be carefully examined, and endorsed by the officers under whose orders the liability was incurred. The claims have to be compared with the original orders, the terms of contract, and quality and quantity of goods

delivered in order to certify their validity. The third and the last step is to make the payment. This is generally done by drawing cheques on the Treasury, or the branch of the Imperial Bank with which the officer has got his public account, though the payments of very small accounts are made in cash, for which the money is drawn in advance by the administrative officer. In meeting these obligations the paying officer has to satisfy himself with regard to the identity of the payees, and obtain the receipts for the amounts paid as an evidence of the fact that the sums charged have been actually been paid.

It is the vital feature of the system of the public expenditure that it should not exceed the appropriations—the amount granted for a specified purpose by the Legislature—together with what has been assigned to it by the chief executive authority (viz. the Governor-General in Council or Governor in Council). It has been already stated that the figures in the budget estimates are assembled according to certain main divisions and their sub-divisions. A grant or a supplementary grant may be in respect of expenditure falling under one or more divisions or sections of a division, though it generally corresponds to main divison known as the major head. It is absolutely essential that appropriations under a grant should be strictly adhered to; and any departure from them is a grave financial offence for which the officers make themselves liable to severe censure. The importance of this rule cannot be exaggerated. It is one of the most important duties of the Finance Departments to lay down regulations for its observance and insist on their being carried out. The accounts of public expenditure are so maintained and examined as to make it easy for officers concerned to enforce it. The controlling officers, who administer a grant or a portion of a grant, have to carefully watch the rate of the expenditure, and if they foresee any excess beyond the appropriations, have to take timely measures to obtain the additional funds from the authority competent to grant them. It is under very exceptional circumstances

that an officer who exceeds his budget allotment can have his action countenanced by the superior authorities. It was stated in the introductory chapter that the financial system of India is efficient; one of the most reliable tests of its efficiency is the extent to which the disbursement of public funds takes place in accordance with appropriations. The cases in which this rule is violated do occur, but they are not very common, and can be easily detected. This is the central fact of the whole scheme of public finance. The Legislature grants specified amounts for specified purposes. It is the paramount duty of the administrative officers to regulate their activities within the sanctioned amounts. The financial apparatus is so constructed as to ensure the proper execution of the budget programme which, as it has been pointed out already, is based on a plan and embodies a policy. It would be impossible to realize the unity of the budget on which so much emphasis was laid in the third chapter, in actual practice, if the spending officers had the discretion to incur obligation not sanctioned or provided for in the budget estimates. It may, however, be added that the want of provision in the budget estimates cannot be cited as a reason for not making inevitable payments. Money which is undisputably payable, cannot be left unpaid because the officer who has incurred the obligation has exceeded the budget appropriations or the limits of his financial powers.

After the budget has been duly passed by the Legislature, or the funds otherwise provided by the Government, the sanctioned amount has to be communicated by the Finance Department to the superior officers of the departments, who distribute it among the subordinate officers, which fact, however, does not affect their responsibility for keeping the expenditure within the appropriations. If the estimates have passed through the Legislature without any material reductions, the communications of appropriations by the Chief Departmental Officer is a simple affair; the estimates having been prepared in detail, the amount needed by each officer can be easily ascertained.

But when the Legislatures have made some lump sum reductions, the task of distributing them requires careful discretion. It is important to remember that the budget assignments are not mandatory. The fact that a charge has been included in the sanctioned estimates does not constitute an obligation for the Government to incur it. There are two conditions necessary for incurring an obligation. The funds must be provided for the purpose, i.e. appropriation made for it. That to the extent to which the expenditure is votable, is the work of the Legislature. But the provision of funds is not a sufficient condition for incurring the expenditure. It must also be sanctioned by a competent authority. Ordinarily the sanction for new expenditure has to be obtained before the charges are included in the estimates, and it becomes operative as soon as the funds are provided for the purpose. But if any departure is contemplated from the budget programme, it is necessary to obtain the sanction before the charge is incurred. The cases in which the proposals of the Central Government and the Provincial Governments in the reserved and transferred departments have to be submitted to the Secretary of State for his sanction, have already been referred to. Each administrative authority has, likewise, got its own well-defined financial powers and within its limits is empowered to sanction expenditure.[1] The sanctions granted by each authority have to be communicated to the audit officers, whose duty it is to make sure that the authority sanctioning the expenditure does not exceed the limits of its powers. For the public works, for obvious reasons, a special procedure has been prescribed. A proposal for expenditure before it is submitted to the competent authority for sanction has to pass through two preliminary stages. It should, in the first instance, be approved by the department for which the work has to be constructed. The department has to say whether the

[1] The financial powers of each officer are given in a publication known as the "Book of Financial Powers," which, however, for some reason which is not easy to understand, is not available for the use of the public.

plan would meet its requirements, and further, whether the cost is reasonable. This is called the "administrative approval" of the proposal. Then the same proposal goes to the Public Works Department, whose duty it is to execute it, and is examined and approved by it from the technical standpoint. By according the "technical approval" the department vouches for the soundness of the proposal as an engineering proposition. This is, however, a variation of the general principle that for incurring expenditure the provision of funds and grant of sanction are both necessary. The sanction is an act of the Executive, and the Legislature has not got anything to do with it. The Government would be within its right to suspend the execution of a proposal or order its retrenchment, in spite of the fact that the Legislature has, by voting a particular demand, provided funds for the purpose. Money is placed by the Legislature at the disposal of the Government, but it is not bound to spend it. If it does not exercise the right before the expiry of the financial year, the grant lapses or becomes inoperative.[1] The lapsed grant, if it is

[1] One result of this rule is that in March there is a rush of expenditure in the Government Offices in order to prevent the lapse of grants. Every year the examination shows how the Government Officers make vigorous efforts to spend as much of their budget allotment as they can, when the year is drawing to a close.

The following table, which is taken from the Audit and Appropriation Report of 1920–21, speaks for itself:

Province.	Percentage of cheques drawn in March to the amount drawn during the year.	Percentage of the amount of cheques drawn during the last three days of March to the total drawn in March.
Baluchistan	35·7	17·8
Delhi	27	11·9
N.W.F. Province	(1) 43·2; (2) 23·2	(1) 24·8; (2) 6·3
Madras	13·3	23·4
Bombay	21·9	25·6
Bengal	21·6	18
United Provinces	23·4	25·2
Punjab	13·7	25·9
Bihar and Orissa	15·6	29·8
Central Provinces	22·7	42·2
Assam	11·8	12·8
Rajputana	19·1	40
Central India	15·9	38·2

necessary to meet the obligations, has to be included in the demand of the next year. The distinction between appropriation and the sanction, which in the case of the non-votable expenditure is a little blurred over on account of the identity of the fund-granting and sanctioning authority, will acquire greater importance as the whole expenditure is made subject to the vote of the Legislature. The determination of the personnel and the scales of salaries by a legislative act is not necessary. The Legislature should grant supplies on the basis of the information given in the estimates, but an attempt to determine in detail the organization of the services would result in very great rigidity, and serve no useful purpose. The Executive being in constant and intimate touch with the working conditions of each service is alone competent to decide matters of detail and adjust the nature of its organization to the nature of the work which devolves upon it. The system combines the merits of adequate control with great flexibility. In the countries in which the Legislature determines the remuneration of each office, and the number of the personnel in each service, the practice creates maladjustment between the needs and the organization of the services and is responsible for great dissipation of the public funds. The Finance Department is expected to exercise financial control over the organization of the services. The nature of this control has been indicated in the Despatch of the Government of India, which has already been quoted so often. It says, "Insertion of a project in the budget means that the Legislature gives the proper executive authority a power to sanction expenditure; it is not an order to disburse money. The order must be given separately by duly empowered authority, and it should not be given without the prior consultation with the Finance Department. At this stage the department can

In the United Provinces in 1920–21 and 1921–22 27·07 per cent and 22·19 per cent of the Public Works expenditure was paid for in March, and 23·4 per cent, 17·96 per cent of the cheques drawn in March were drawn in the last three days of the month. The Public Works Department is the worst sinner in this respect.

scrutinize and advise on details which were not probably available at the budget stage ; and it has also to see that funds allotted in the estimates for non-recurring expenditure are not employed so as to involve recurring expenditure which has not been foreseen." It is necessary to appreciate the difference between the grant of funds by the Legislature, and their application by the executive authority. There are two distinct financial acts, intimately connected with each other, but still each has got its own special significance in the working of the financial system.

The Legislature grants the total sum required for the service defined in the title of the demand, and is not concerned with the sub-heads except as justifying the total. The members can, of course, propose a reduction of the total by the sum included in the estimates for some specified purpose. If such a motion is carried, the Government would be precluded from spending money for that purpose ; but as that does not alter the fact that money is voted for the whole service, and is classified in the sub-heads merely for the convenience of the members. The grant cannot be exceeded without the express approval of the Legislature. It is watertight. The funds sanctioned for one grant cannot be transferred to another. That requires the legislative sanction. But within the amount of the sanctioned grant, the Government possesses full powers of transferring from one unit to another by a formal order of what is technically called the reappropriation. Re-appropriation or the diversion of funds from one unit to another gives to the system of appropriations an elasticity which, in view of the fact that the budget estimates are prepared months before they go into effect, is highly desirable in the interest of economy and efficiency. Everything cannot be foreseen, and when new developments take place, it is possible for the Executive to make the necessary adjustment by utilizing economies under one sub-head for meeting increased expenditure under another. In the absence of this power the estimating officers would be tempted to estimate more liberally under every sub-

head to avoid the danger of deficiency in any, with the result that their aggregate spending power would be augmented, the Legislature would have to sanction many more supplementary grants, as every unexpected increase of expenditure would require its approval, and one of the effective incentives to economy would be removed. The importance of the last consideration can be readily understood, when it is borne in mind that the lapsing of the unspent surpluses of every grant at the end of the year leads to hasty and uneconomical expenditure when it is drawing to a close. If the unexpended balance of every major head, minor head, and the unit of appropriation included in a grant has to be surrendered to the Treasury, the situation, it can be easily imagined, would become much worse. With the approach of the end of the year, the state of unexpended funds would be carefully examined with the deliberate purpose of seeing how all the available money can be easily used. Each service has got its *esprit de corps.* Any money that has to be returned to the Treasury would be considered a loss to the service for which it was originally appropriated. The economies which are now effected by saving money on one subdivision of service in order to spend them on another would not take place, and what happens in the case of one grant as a whole, would happen to every unit of appropriation. It is not necessary to add that the situation as a whole would not make for the economy of expenditure.

There is, however, no denying the fact that the practice of reappropriation has, in spite of its manifest advantages, dangers of its own. It is necessary to provide safeguards against the abuse of this power. An unwarranted use of this power is likely to defeat the purpose for which the appropriations are made. The officers may fall into the habit of inaccurate estimating because they know that the deficiency in their peculiar domain can be easily made up by the diversion of funds under other branches of the service, the existence of the surplus in which they are likely

to take for granted. It is possible that the grant of discretion to the administrative officers would expose them to the pressure from the interested quarters, to whom the prosecution of a work in one section of the country rather than another may be a matter of some consequence. The use of this power has, therefore, to be jealously watched in actual practice. In the United Kingdom two safeguards have been provided. In the first place each reappropriation requires the sanction of Treasury, which, as already stated, is an organ of financial administration independent of and superior to other spending departments, and can therefore exercise comprehensive financial control and prevent the abuse of this power by the administrative authorities. The changes in the allotment of funds are made by the formal action in writing, and have to be recorded in order to show how far the original scheme of appropriations has been modified. It is the duty of the Auditor-General and the Public Accounts Committee to examine the circumstances of transfer in each individual case, and report on the propriety of the departure from the allotments specified in the estimates. In India each act of reappropriation either requires the assent of the Finance Department, or has to be made with its knowledge. It is also necessary here for the Audit Officers and the Public Accounts Committees to examine all such cases and report them to the Legislature. It is not possible to say how far this double check is an effective safeguard against the abuse of this discretionary power. In the United Kingdom its efficacy is admitted by the authorities whose right to form an opinion on the matter cannot be questioned. In India its adequacy will depend upon the traditions which the Finance Departments, both central and provincial, develop in the course of time, and the independence and ability with which the audit is conducted by the Audit Department, and the financial operations of the year are reviewed by the Public Accounts Committees. The transfer of funds from one grant to another in case of the non-votable items can be made with the con-

sent of the Finance Department. The transfer from a non-voted head to a voted head is not allowed under any circumstances, as that would obviously weaken the control of the Legislatures over the items submitted to their vote; for the Government can by the use of this power spend money in excess of the budgeted allotment for heads for which the Legislature has granted particular amounts that are not to be exceeded on any account. The reverse process of transferring to the non-voted from the voted heads is admissable as far as the provinces are concerned, and can be sanctioned by the Finance Department, if the Provincial Government anticipates a lapse under the voted head, or there is an actual surrender from the voted grant. All reappropriations between the major and minor heads require the sanction of the Finance Department in case of the expenditure from the provincial revenues. The Ministers and the Members of Executive Council can sanction reappropriations subordinate to a minor head provided no recurring liability is incurred thereby and the units are under the charge of the same Minister or the Member. A copy of the order of reappropriation has always to be sent to the Finance Department as soon as it is passed. This power can be delegated by the Minister or a Member to any subordinate officer with the previous consent of the Finance Department.[1] Reappropriations cannot be made for an object not specifically included in the estimates, nor to increase an expenditure on an object if the expenditure originally proposed in the estimates has been reduced by the Legislative Council or the Government as the case may be.[2] The power of reappropriation is not centralized in India to the same extent as in the United Kingdom, but the control exercised by the Finance Department is fairly extensive, and should, if properly exercised, check any tendency on the part of the spending

[1] *Vide* Devolution Rules, Rule 38.

[2] The powers of reappropriation of the funds provided for from the central revenues are also given in the "Book of Financial Powers," which, as already stated, is treated as a confidential document.

authorities to rely upon reappropriations as ordinary means of obtaining funds.[1]

[1] The Finance Departments, the central and the provincial, have besides the power of authorizing reappropriation at their disposal, unallotted reserve which can be drawn upon when the need is urgent, and funds for the purpose cannot be provided in any other way. The amount of this reserve in the case of the Central Government is 3 lacs.

CHAPTER VIII

WORKING OF THE TREASURY SYSTEM

THE English Exchequer has been defined as the purse of the nation. In India there is no one purse for receiving and making payments, but there is an organized system for receiving and issuing money, which is suited to the Indian conditions. There is a Treasury in every district to which are attached a number of sub-treasuries. Besides the treasuries the Imperial Bank with its branches is an institution for doing the financial work of the Government. The treasuries and the branches of the Imperial Bank are inter-related and work under the direction of the officers, who take their orders from the Finance Department of the Government of India. There are about three hundred treasuries and twelve hundred sub-treasuries, three local head offices, and ninety branches of the Imperial Bank. They, taken together, constitute what may be called the financial nervous system of India. They receive the stimulus from contact with the concrete facts, convey the messages to the centre, and receive the command to act. The response to the stimulus is ordinarily automatic. The local centres can be left alone to carry on the financial work according to the standing regulations—the official registrations. But when there is need for readjustment or co-ordination among the different centres, the intervention of the central authority is necessary. The system is well-regulated and so designed as to embrace all the financial operations of the Government.

It is an essential principle of our financial organization that appropriation of departmental receipts to meet departmental expenditure, unless specially authorized, is strictly

prohibited. Cash realized by the revenue collecting departments and the receipts of railway, public works, military, and the civil departments have to be paid into the nearest Treasury as soon as possible. Funds for meeting expenditure have to be drawn from the Treasury separately and accounted for in the ordinary manner. As an exception to the general rule certain officers are allowed to cash cheques against their drawing account from their departmental receipts, the former being paid into the Treasury in lieu. This exception is made in the case of those officers, for whom the observance of this rule would be a source of inconvenience to all concerned. When any person has an occasion to pay money into a treasury, he usually procures a document known as the Chalan, enters therein the nature of the payment as well as the name of the person or the officer on whose account the payment is to be made, has it checked, passed, and recorded by the Revenue Department, and then pays the amount into the Treasury, and gets the necessary receipt. This Chalan is in duplicate, one copy being retained in the Treasury for record, the other given to the payee as a receipt. It is not the duty of the Treasury Officer to see that the dues of the Government are regularly paid. That is the work of the departmental officers. The Treasury Officer is concerned with the regularity of the transaction, and has to satisfy himself that the document, on the basis of which the payment is being made, is in order. The superior officers of the revenue departments receive from the Accountant-General the extracts from his accounts showing the amounts brought to credit on account of their departments, which they are to compare with the accounts and returns received by them from their own subordinates. The Treasury, having received the amount, brings it to account and money becomes part of the general balances of the Government, and is available for meeting all public obligations whatever their nature. It is important to remember that the receipts in the treasury are not earmarked for any special purpose. In the accounts they are credited to certain heads and are

shown as being part of either the central or provincial revenues as the case may be, but these are merely book entries. All receipts are pooled together, and are used for making all payments of *bona fide* character. The advantage of this amalgamation of funds is obvious. It obviates the necessity of keeping separate balances for the spending department, makes it possible for the Government to reduce their aggregate amount, and also to devise a satisfactory arrangement for their safe custody.

Payments from the Treasury are either final payments or imprests, i.e. advances. They are made either on behalf of the Central Government or Provincial Governments. The greater part of payments made by the treasuries for civil and the public works departments are of a simple character and final. The Accountant-General places the officers in account with the treasuries, authorizes the Treasury Officers to honour cheques drawn or bills presented by them, and the spending officers to issue drafts on the treasuries up to the limit of their appropriations. That they do not exceed their budget allotments is watched by the controlling officers and the Accountant-General to whom the accounts are subsequently submitted for audit. The Treasury Officers submit in support of their accounts the proofs of final payment, the receipts of the payees, together with the bills or any other document on which the payment is claimed. The military, the railways, the forest, the posts and telegraphs and other departments, which have their transactions all over the country and are working under the direct control of the Central Government, however, draw lump sum amounts from the treasuries by drawing cheques on them, and the actual payments are made by the disbursing officers of the departments. The Accountants-General, or in some cases the Controller or Deputy-Controller of Currency, issue to the treasuries concerned what are called the letters-of-credit in favour of the departments concerned, authorizing them to make payments to their disbursing officers up to a specified amount. In issuing these letters-of-credit they have

to make sure that the amounts so assigned did not exceed their budgeted allotments. This method involves a double check on the payment issues. The controlling officers and the audit officers watch the progressive totals of expenditure debited against a particular grant, and provide for anticipated excesses if any ; but inasmuch the assignments granted to the disbursing officers on the letters-of-credit are always within the sanctioned amounts, it is practically impossible for them to exceed their appropriations in incurring public expenditure. "It is an essential feature of the arrangement that the payments at any stage do not exceed the proportionate provision made to date in the assignment."[1] The Treasury Officer submits in support of his accounts the cheques drawn by the disbursing officers of the departments, who have to account for the money by submitting bills and proofs of payment to their audit officers. The procedure for getting money from the Treasury is simple. When a bill or a cheque is presented at a Treasury it is checked by the accountant and laid before the Treasury Officer, who, if the claim is *prima facie* admissible, issues the authority to pay. The treasurer then pays the required amount across the counter, and obtains the payee's receipt as a proof of payment. The responsibility for an overcharge rests primarily with the drawer of the bill and the officer who countersigns it for payment. The Treasury Officer has, however, to check all palpable errors and decline payment of all claims which are not covered by the regulations. All charges in due course come before the Audit Officer, who, if any charge is irregular or in excess, instructs the Treasury Officers to remove the irregularity or recover the excesses. In a few cases the officers are allowed to have fixed advances out of which they make small and casual payments. The officers drawing advances have to render account of the amount drawn by them and recoup the advance when it gets depleted by issues. The Government of India is re-

[1] *Vide* Introduction to Indian Government Accounts. Second Edition, para. 58.

sponsible for providing money for all public charges. In forecasting its ways and means position in the ensuing year, it lays out its programme with a view to have adequate funds for all charges that can be foreseen. For this purpose it takes into account the anticipated expenditure of the Provincial Governments as well as its own, and makes provision to meet it. During the currency of the year the position has to be watched with a sedulous care. Each Treasury is stocked with cash that it will be called upon to pay, and the solvency of the Government as a whole is safeguarded by insuring that the funds will not fall short of public requirements. The actual payment is made to the Treasury Officers, but the responsibility for seeing that he is provided with sufficient funds devolves upon the Controller of Currency, who is the agent of the Finance Department of the Government of India.

In the foregoing paragraphs nothing has been said about the part which the Imperial Bank plays in the receipt and issue of public money. The Presidency Banks, out of which the Imperial Bank has grown, were always associated more or less intimately with the financial work of the Government of India, but the Imperial Bank has been constituted with the avowed purpose of making it in due course the State Bank of India. The part which it will play in the future financial organization of the country (giving the phrase an extended significance, and taking it to comprehend our monetary, currency, banking and fiscal institutions) cannot be predicted, but that it will acquire a greater importance in the financial organism may be taken for granted. But here we are concerned with its present position, and that is that every station where there is a local head office or a branch of the Imperial Bank all Government receipts are paid into and the issues made by the Imperial Bank. There are three local head offices, and there is a provision for opening more, and there are about ninety branches, and more are being opened every year. The procedure for dealing with the financial transactions varies according to the authority through whom the

Government authorizes the Imperial Bank to receive or issue money on public account. Receipts are paid on Chalans, or the memorandum of particulars, which are in the first instance presented at the Treasury, where the officer in charge examines it, enters the amount in his books, certifies its correctness, and specifies the head of account to which it is to be credited. The Chalan is then taken by the payee to the Imperial Bank, where the amount is received and duly credited, and the acknowledgment granted to the payee. The claims for payment are similarly scrutinized by the Treasury Officers, passed by them, entered in the books of the Treasury, and then presented by the person concerned to the bank for payment. The agent of the bank is responsible for strict adherence to the orders of the Treasury Officers and has nothing to do with the regularity or otherwise of the transaction. The departments which draw funds on the letters-of-credit get money from the bank against their own assignment, and make their own disbursements. Every day the agent of the bank sends to the Treasury Officer a classified list of the receipts and payments of the day before, supported by necessary documents, which the Treasury Officer has to compare with the entries in his accounts in case of the transactions which pass through his hands before they are dealt with by the bank, and examines others carefully to see that everything is in order. Each item of receipt and payment is then posted in the Treasury account. The unspent balances of the Government of India are left in deposit with the bank for which the latter does not pay any interest. Before the formation of the bank it was the complaint of the commercial community and the students of the Indian Currency System that the existence of the independent treasuries, which were completely divorced from the business life of the community, led to the withdrawal of a very large portion of the liquid resources of the country from circulation and their lock-up in the Government treasuries. This generally happened at a time when the need for the expansion of currency was particu-

larly great, as the period of trade activity and the collection of revenues by the Government generally synchronized. The effect of the system was to produce very great financial stringency, which sent up the discount rate or the price which the merchants have got to pay for the short term loans. Our currency system is not sufficiently elastic to prevent very great rise in the discount rate, but the incapacity of the credit to respond adequately to the need for the currency expansion is not mainly due to the withdrawal and the lock-up of the cash resources of the country. The figures given in the next chapter will bear out this statement.[1] The difficulty has not been completely overcome, but it has been diminished. As more branches of the Imperial Bank are opened and the financial work of the Government is taken over by them all the Treasury balances of the Government will form part of the banking reserve of the country and be available through the Imperial Bank for the use of the business community. As the economic life of the country becomes more complex—as it must—with the development of our internal and external trade, the need of establishing complete harmony between the business and the fiscal organization will grow in importance. The existence of a well-managed bank will be of very great advantage for achieving this end. But if the institution is to serve any good purpose it must be regulated by the public authority. The Imperial Bank, as at present constituted, has four members of the Central Board (which is the chief executive body of the bank) nominated by the Government, and the Controller of Currency is its *ex officio* member and has the power of staying its proceedings when he thinks the public interests are in any way endangered by the policy of the Board. The arrangement has not been at work long enough to afford any evidence for or against the sufficiency of the public control of the institution ; but if the experience shows that the interests of the tax-payer, whose money it uses, suffer for want of adequate supervision, the whole constitution will have to be revised before

[1] *Vide* Chapter IX, page 236 footnote.

the bank is allowed to assume a more important place in our financial organization than it now occupies. The present constitution has been devised on the express recognition of the fact that no Government can nowadays afford to leave the economic life of the country severely alone in working out its fiscal arrangements. The Imperial Bank is now the fiscal agent of the Government of India.

Every Treasury Officer has early in every month to submit the statements of the total sums received and issued up to the close of the preceding month to the Deputy Controller of Currency, who consolidates the statements of the treasuries situated in his jurisdiction and forwards the consolidated statements to the Controller of Currency. The latter officer prepares consolidated statements of the income, expenditure and cash balances of the whole country on the basis of the statements of the Deputy Controllers of Currency, and places them before the Finance Member. "The early information derived from the preliminary reports, supported by the fuller information which follows without undue delay enables the Finance Member of Council to keep his finger on the financial pulse."[1] He has the opportunity of knowing in time how far the receipts and expenditure correspond to the budget estimates, and if there is any appreciable divergence between the actual and estimated figures, he can locate it with precision and analyse its causes. If the receipts are increasing or the expenditure is below expectations, the outlook is distinctly cheerful for him, and he can by changing the borrowing programme, or in some cases increasing his capital outlay use the unexpected surplus to some advantage. If he cannot find an immediate use for his surplus he can contemplate the possibility of the closing balance being somewhat higher than what he budgeted for with complete equanimity. But if unfortunately the receipts are falling off or the expenditure is in excess of the anticipations, the situation is less reassuring and makes readjustment imperative. He can

[1] *Vide* Welby Commission Report, Vol. IV, para. 51.

take the necessary action by ordering the reduction of expenditure if possible by increasing the amount raised by loans, by renewing the old loans which would otherwise have been paid off, or by process of inflation—a word which, on account of the world-wide use of this device, has become quite familiar, i.e. by printing more currency notes without a sound basis. The point which deserves special notice is that the concentration of receipts and issues in the treasuries enables the Finance Member of the Government of India to keep the situation well in hand, and if there are any developments which call for change of financial policy or of the ways and means programme, the necessary action can be taken promptly and without delay. The unexpected may happen with an amount of suddenness as to take him unawares, but it is exceedingly unlikely that such a contingency will occur. The Finance Member can always depend upon getting timely warning regarding what is coming in the near future and shape his policy with a view to meet the new developments more than half way. The utmost care is taken in the preparation of the estimates. The financial programme is drawn up on the basis of the forecast of those who by experience, training and the nature of the duties which they perform are in a position to take the prospective view of the matter. But if in spite of all this surprises come—and it is impossible to prevent them—the working of the Treasury system holds out the danger signals sufficiently in advance to enable the pilot to change the course of the vessel and keep it off the impending difficulties. Nothing is left undone which can be of any use in intelligently foreseeing the financial situation and retaining its mastery when things are taking their own course.

It is of some importance to describe the organization of a Treasury to get a clearer idea of its working. A Treasury consists of two departments: one of accounts under the charge of an accountant, and the other of cash under the charge of a treasurer. The Treasury is in the general charge of the collector, who entrusts the immediate

executive control to a Treasury Officer subordinate to him, though he cannot thereby divest himself of his administrative responsibility. The treasurer actually receives and issues money, and is, conjointly with the Treasury Officer, responsible for the safe custody of cash. He maintains a register in which each transaction of receipt and payment is posted as it occurs. The accountant has got a register of his own in which the same transactions are brought to account. He also posts in his register the daily sheet of each sub-treasury of receipts, payments and balances of the day before (and in some cases of two days before, according to the distance of the sub-treasury by post). At the close of the day the Treasury Officer checks the two registers, together with the supporting documents, sees whether they agree with each other, verifies the cash in hand of the treasurer, which is then lodged in the strong room for safe custody. The cash on the last day of the month is verified by the collector, or in his absence by a responsible officer to whom he assigns this duty,[1] and a cash balance report is prepared and forwarded to the Deputy Controller of Currency. At the close of the month an account of total receipts and issues is sent to the Accountant-General accompanied by the supporting documents. The organization of the sub-treasuries is similar to that of the Treasury. They are primarily intended for being the depots for collecting revenues, but are also used, to a limited extent, for making payments. The officer in charge of the sub-treasury works under the direct supervision of the Treasury Officer of the district treasury, and the cash balance report is prepared for the whole district. The Treasury Officer works under two masters, and if the collector is taken into account, under three. In matters of audit and accounts he is under the Accountant-General and through him the Auditor-General. In matters of the provision of funds and their transfer from one Treasury to another he receives his instructions from the Deputy

[1] The Collector, however, must perform this duty in person at least once in every four months.

Controller of Currency and has to obey his orders. Once a year every Treasury is inspected by an officer of the Audit Department. It is the duty of the Inspecting Officer to see whether the procedure prescribed for the observance of Treasury Officers regarding the custody of funds, posting of cash books and other registers, verification of cash balances, examination of claims for payment, and other cognate matters is strictly adhered to. A report of the result of inspection is prepared in two parts, one relating to matters administered by the Deputy Controller of Currency and the other dealing with all other points. The section of the report which pertains to matters in the charge of the Deputy Controller of Currency, is disposed of by him, and the other is dealt with by the Accountant-General. The collector is expected to take the necessary action on points which are made subject of adverse criticism in the two sections of the report of the Inspecting Officer, and submit his own report to the Deputy Controller of Currency and the Accountant-General. These officers bring to the notice of the higher authorities all matters in which, in their opinion, the action taken by the collector is inadequate. The inspection does not in any way affect the responsibility of the revenue authorities for the proper management and working of the district treasuries. The object of the inspection is to stimulate their sense of responsibility and bring to light the defects which would otherwise remain unnoticed. The district treasuries are the units of the fiscal system, and it is of vital importance that their efficiency should remain unimpaired, and their activities co-ordinated by officers who have broader outlook and can distinguish matters of broad policy from the minute details, which make up so much of the official routine.

There is one point which is not of immediate practical importance but is interesting from the theoretical standpoint. In England the procedure for making payment issues is very elaborate, the object of which is to secure that no issues shall be made from the Exchequer by the Executive

for purposes other than, or for amounts greater than those that have been authorized by the Parliament. All receipts are deposited in the Bank of England in the Exchequer account, which is in charge of the Auditor and Comptroller-General. He holds the fund on behalf of the Parliament, and any issues out of it are made under his authority. The Treasury secures formal authority from the Auditor and the Comptroller-General to requisition funds. It has to secure credits upon the Exchequer account which are granted if the requisition is in order and covered by appropriations. The Treasury then authorizes the transfer of funds from the Exchequer account to the Paymaster-General, who performs duties analogous to but simpler than the duties entrusted to the Controller of Currency in India, and specifies the purpose and the amount for which the issues are to be made. The spending officers then make out drafts on the Paymaster-General, who authorizes them to draw money from the Bank of England. The funds transferred to his account follow the classification of the votes but constitute a general balance out of which he makes his payments. The purpose of these formalities is to enforce strict adherence to the scheme of appropriations sanctioned by the Parliament. It has been suggested that a system similar to the system of the Exchequer issues in England should be introduced in India to secure more complete and efficient control over payments. The object can be achieved if all revenues, which are collected on behalf of the Secretary of State, were placed under the exclusive control of the Auditor-General, who, or his assistants, should transfer funds to the credit of the Controller of Currency by extending the system of issuing letters-of-credit to all departments in which the purpose and the amount for which the issues are to be made by the Treasury Officers should be specified, the Treasury Officer for this purpose working under the orders of the Controller of Currency. This suggestion, interesting as it is, is a little in advance of the facts of our political system. The Indian revenues are collected not on behalf of the Indian Legis-

lature but the Secretary of State in Council. The system of the Exchequer issues would give still greater prominence to his authority in our fiscal arrangements. It is not desirable to set up such a complicated system, which will have the effect of emphasizing the financial supremacy of the Secretary of State still further, when it is acknowledged on all hands that the future changes in Indian polity must have the effect of decreasing his intervention in the Indian affairs. When the Indian Legislature becomes supreme in financial matters, and the Auditor-General responsible to it, it will be time to think of introducing a system of payments, which may prevent the issue of funds except under its authority. But when 55 per cent of the central and a portion of the provincial expenditure is outside the control of the Indian Legislatures, the Governor-General and Governors possess the power of incurring expenditure in spite of the disapproval of the Legislature, and the whole income is collected in the name of the Secretary of State, it is premature to introduce a system, which in the country of its origin is designed to assert the supremacy of the sovereign Legislature. As far as the purpose of preventing the issue of money from the treasuries in excess of the sanctioned grants is concerned, the system of issuing letters-of-credit in favour of the departments which are not under the audit control of the civil Accountant-General is quite effective, and it is not necessary to introduce it for ordinary routine payments of the civil departments whose monthly accounts are audited by the Accountants-General within a few weeks of their completion. In the case of the Public Works Department, which has got to make large payments, it may be desirable to secure a more efficient control over its expenditure by bringing the drawings of the spending officers in respect of some important works under the operation of letters-of-credit. In England the system of the Exchequer issues is the relic of old historic antagonism between the Crown and Commons. Its utility, now that the Executive is completely responsible to the Parliament, has been questioned. In India the line of evolution is to

establish the responsibility of the executive to the Legislature.[1]

The Governor-General in Council has been empowered under Rule 10 of the Devolution Rules to prescribe, with the previous consent of the Secretary of State in Council, "procedure to be followed for the payment of moneys into and withdrawals from public accounts, and for the custody of moneys standing in that account." Under the rules the Governor-General in Council has issued the Treasury Orders, which govern the procedure of the treasuries.[2]

[1] The Public Accounts Committee of the Central Legislature, in their report on the Appropriation Report of 1921–22, after emphasizing the importance of stopping all irregular expenditure, make the following comments:

"In this connection the question was raised of the possibility of preventing excess expenditure by making it impossible for spending officers to get money in excess of a certain fixed sum without proper authority. We understand that there are great difficulties in the way of an absolute control in this matter owing to the large number of disbursing centres in India at which money has to be made available for expenditure. The matter, however, is so important that we recommend that the suggestion should be carefully considered by the Government."—*Vide* Public Accounts Committee Report, para. 20.

The Government of India has arrived at the following decision on this recommendation:

"The question will receive careful consideration of the Government of India. But there are some practical difficulties owing to the existence of a large number of disbursing centres. For the present the Government of India has directed that the steps should be taken by the various Departments of the Government of India to impress on the disbursing authorities the absolute necessity of obtaining funds from the Legislative Assembly, for voted items of expenditure and from the Government of India for non-voted items before any expenditure is incurred. They should obtain the previous approval of the Finance Department, when for reasons of emergency it is proposed to incur voted expenditure in anticipation of a supplementary vote."

[2] *Vide* Appendix V.

CHAPTER IX

BALANCES AND RESOURCE OPERATIONS

Every Government must have some cash in hand. Under certain circumstances it may be justified in budgeting for a deficit, but a Government which budgets for a minus working balance proclaims, thereby, its inability to meet its obligations. It becomes insolvent. The Government of India has to find money for liabilities of all kinds. It has to pay its permanent servants, civil and military, it has to pay its contractors, it has to repay the loans which have matured and pay interest at regular intervals on all outstanding loans, it has to pay money to the Postal Savings Bank Depositors who are entitled to withdraw it at call, it has to provide cash for the expenditure of the Provincial Governments, it has to finance its capital undertakings, and it has to meet its liabilities in English currency. Cash in India has to be provided not at one paying centre but at all the district treasuries and sub-treasuries, and sufficient balance has to be deposited at the Imperial Bank to enable it to make all Government disbursements through its head offices and branches. The complexity of this network of operations can be easily realized if we take into account the number, magnitude, and diversity of the payments, and the extent of the country over which they have to be made. The fact that a very substantial portion of these payments are incurred in England and have to be paid for in English currency makes the situation still more complex, and has been and is still a great disturbing factor in the Indian finances. The ways and means programme of the Government of India comprehends, it has already been made clear, all receipts whether from taxes, quasi-commercial enterprises, repayments of loans advanced to the subordinate author-

ities, proceeds of the new loans floated in the year, balances of the Provincial Governments and all local bodies, and the Postal Saving Bank Deposit, and all disbursements whether for expenditure chargeable to revenue, capital outlay, repayments of loans, provincial overdrafts, advances of loans to the Provincial Governments and the local bodies, and withdrawal of the Postal Savings Bank Deposits. The object of the ordinary budget is to forecast the regular income of the State from taxes and other ordinary sources of revenue, and lay it out to the best advantage. The ways and means budget, on the other hand, anticipates all outgoings, and provides for them by making the incomings, whatever their source, adequate to cover them. As the Finance Member put it in his budget speech of 1923: "Money to meet the outgoings has to be got in before it goes out." The coming in of money depends upon a number of factors. It depends upon the monsoon, harvests, activity of trade and commerce—the factors upon which the yield of taxes depends—and, what is still more incalculable, the changing conditions of the money market in India and in England. The incomings may be disappointing. The rate at which they come or their total amount may be different from the budget anticipations, or at a particular time the outgoings may be heavier than the incomings.[1] Provision has to be made for all these

[1] In the first four months of the year the receipts are in excess of disbursements. During May and June the receipts fall off, but still the balances are generally large. But from July to November the receipts fall short of the demands on the treasuries and the balances run low. In December the balances are generally at the lowest point. The subjoined table showing the treasury balances on the first day of each month for the years from 1917–18 to 1922–23 bears out the above remark:

Table showing the Treasury Balances in India on the first day of each month from 1917–18 to 1922–23 (in thousands of rupees):

Year.	Jan.	Feb.	March.	April.	May.	June.
1917–18 .	16,79,48	22,84,42	25,25,57	22,93,98	24,72,64	32,48,70
1918–19 .	14,72,60	15,75,86	19,21,22	22,98,77	17,47,72	19,86,23
1919–20 .	14,06,44	29,15,31	29,13,57	25,96,81	21,67,62	16,22,01
1920–21 .	15,15,48	13,43,67	11,99,15	26,47,60	25,39,79	28,45,92
1921–22 .	11,18,27	15,87,48	18,08,37	13,83,57	19,73,89	18,80,30
1922–23 .	17,61,02	22,01,74	21,52,60	25,66,13	19,69,78	20,82,31

contingencies, and it is done by maintaining a certain amount of cash in hand as a reserve, which can always be drawn upon to meet all the liabilities. The treasury balances constitute that reserve. They consist of balances of all treasuries and sub-treasuries, balances in the Imperial Bank, and the balances of the Secretary of State, which are deposited in the Bank of England, or lent out for short periods.[1] The ways and means budget provides for sufficient closing balances, which are not allowed to fall below a particular minimum. This minimum amount is composed of two sections, the minimum which is to be maintained in India, and the minimum to be maintained in England. The estimates of the minimum amounts here and in London are based on experience. The balances in India are carefully watched from time to time, and if there are any indications of their being reduced below the minimum, the steps are taken to replenish them in some way or the other. The monthly cash balance report of the Treasury Officers has already been referred to. That is submitted on the first working day of the month. Besides this monthly report, three reports giving the total Treasury balances of the district have to be submitted on the 7th, 14th, and 21st of each month to the Deputy Controller of Currency. Besides the monthly report, which is submitted on the prescribed form and gives full details, the Treasury Officer has to telegraph to the Deputy Controller of

Table showing the Treasury Balances—*continued.*

Year.	July.	August.	Sept.	Oct.	Nov.	Dec.
1917–18 .	39,96,25	25,46,92	26,46,92	20,73,75	18,58,08	16,51,70
1918–19 .	23,36,03	16,16,69	14,89,62	27,65,95	16,89,18	13,66,18
1919–20 .	16,49,84	15,55,92	16,78,85	14,18,41	18,73,03	19,53,38
1920–21 .	25,74,16	28,76,18	25,79,10	24,20,65	18,95,94	13,29,40
1921–22 .	27,68,39	30,93,37	16,81,09	13,33,33	13,77,02	16,14,54
1922–23 .	20,91,56	37,17,95	30,68,54	17,11,85	16,72,00	16,78,85

[1] Out of the cash balances in England a working balance of about £500,000 is held at the Bank of England and the remainder is invested for short periods varying from three to four weeks. The investment is made by the Accountant-General of the India Office through a broker who is a very highly-paid official of the Government.

Currency the total treasury balances in the district on the last day of the preceding month[1] and the amounts deposited in or withdrawn from the Imperial Bank. These reports, when consolidated, give information as regards to total cash balances in the country. The size of these balances, it need not be added, is no index of the soundness or otherwise of the financial situation. The balances are a reservoir fed by many streams.[2] It may be full because a lot of money has been borrowed by the Government or deposited by those who bank with the Government of India or it may be comparatively empty on account of the capital outlay from revenues and loans or other disbursements, which will constitute assets of the State in the long run, having been particularly heavy. The soundness of finances depends upon the public expenditure being wisely incurred and not allowing its total amount to exceed the national revenues. The size of balances is determined by a number of circumstances which may, from the point of view of the ultimate financial stability, have different significance.[3] But that does not mean that their size is

[1] The cash balances of the sub-treasuries are included in the report. Their monthly accounts are closed a day or two before the close of the month to enable the sub-treasury officers to communicate to the district treasury the state of balances.

[2] In this connection description of cash balances given by Sir Fleetwood Wilson is worth quoting. He once said: "As the Government of India is its own banker, it is into our general cash balances that all our current revenues are paid and from that all our current expenditure is drawn. They are also the reservoir for the proceeds of all sterling and rupee loans, whether raised by the Government or by railway companies which work our State lines, for the whole of our unfunded debt, and for all the miscellaneous deposits which are not earmarked for separate custody. All the provincial balances merge in them, and in them are absorbed all the repayments and interest on State loans and advances to local bodies and private individuals. Similarly it is out of our cash balances that we take all our capital expenditure on railways and irrigation, all the advances which the Government makes to the local bodies and private individuals, and all the money used in the discharge of our permanent, temporary, and unfunded debt or in the repayment of deposits. Finally it is through our cash balances, owing to their being located partly in England and partly in India, that the Council Bills are usually drawn and the greater part of Government remittances between England and India are effected. It is with our cash balances, therefore, that our estimates of ways and means are concerned."

[3] During the five years of the deficit, 1918–19 to 1922–23, the balances have been quite large. The treasuries were full, but the State was, during these years making what the Finance Member called the rake's progress.

a matter of no importance. A Government which wants to keep its credit intact must be prepared to meet its liabilities. Its failure to pay the claims may shake the public confidence, in spite of the essential soundness of national finances, and have consequences of a far-reaching character. The credit of the Government, like the credit of the banks, depends upon the promptness with which the claims are met. The delay may be fatal; and once the credit receives a shock, it takes a long time and watchful care to build it up again. The maintenance of sufficient balances is, therefore, necessary to make it possible for the Government of India to be always ready to make all Government disbursements from day to day. If, however, unduly low balances carry with them the risk of the Government being exposed to the danger of undermining public confidence in its ability to pay, it is a common-sense consideration that they should not be unduly high. It is held, and rightly, that in these days of banking, security of life and property, and opportunities of profitable investment, it is not wise for the individual to keep more money with him than what is needed for meeting immediate requirements. It is folly to hoard money and let it lie idle when it can be made to fructify by judicious investment. The Government can always find good outlets for laying out its balances, if they tend to grow excessive, but apart from the wise application of funds, the maintenance of balances over and above the amount of what is necessary for safeguarding public credit involves additional expense. It means loss of interest on money that is lying idle in the vaults of the Treasury (the Imperial Bank does not pay any interest on public deposits), its custody involves trouble and expense, and the possibility of the misappropriation of funds is increased in proportion to their magnitude. The amount which is adequate and no more than adequate for public purposes cannot be determined on *a priori* considerations. It depends upon the amount of the Government disbursements, the circumstances under which they are made, and the general economic

development of the country. The Government in England generally does not maintain large balances of its own. There the payments are centralized. The Government can always depend upon raising temporary loans from the public, and getting temporary advances from the Bank of England, when the disbursements are larger than receipts. The Government of India has, on the other hand, to make payments all over the country, and in spite of the gratifying improvement in the lending capacity of the public and the banks in the recent years, the description of the Indian money market by Sir David Barbour, in his evidence given in London before the Welby Commission in 1895, still holds true to a very large extent. After pointing out how the Government of India worked with its own balances, he went on to say, " You see that in India there is not the great supply of the loanable capital that there is in this country, in London, nor can you get loanable capital from outside very readily ; and the transactions are carried on much more by cash than by credit, so that any increase of capital or demand, not in itself very great, leads to a scarcity of cash. Therefore we cannot depend upon the market ; we must keep a balance."[1] Loanable capital has since 1895 increased, the expansion of banking credit has taken place, and the recent amendments in the Paper Currency Act make it possible to ease the money market by lending the currency notes to the extent of 12 crores[2] on the basis of the genuine trade bills, and thereby afford a partial relief to the business community ; but it still remains true that the Government of India cannot safely rely on the money market, and it must have a balance of its own and a large one for the matter of that. But making allowance for all these considerations, it has to be admitted that the Government of India has several times

[1] *Vide* the Welby Commission Report, Vol. I, p. 2016.

[2] According to the Paper Currency Amendment Act of 1923 the Controller of Currency has been authorized to advance money up to the maximum of 12 crores to the Imperial Bank on the security of the internal bills of exchange. The amount which can be lent at a particular time varies according to the bank rate. As the bank rate rises, the amount lent is increased till the maximum of 12 crores is reached.

been known to let its balances grow disproportionately large.[1] The size of the balances and the location of a very large portion in England a few years before the outbreak of the war were made a subject of adverse criticism, and the Chamberlain Commission was specially asked to make enquiries into the matter. The Chamberlain Commission exonerated the Government from any serious blame, and attributed the large amount of the Treasury balances and their distribution between India and England to circumstances, which could not be foreseen and over which the Government of India has no control. They, however, commended the practice of giving loans for short periods in India for the acceptance of the Government of India to avoid hardship to the business community, which resulted from the lock-up of the public funds in the Government treasuries. The outbreak of the war made it necessary for the Government of India to postpone the formulation of a definite policy in this respect; but during the war the Government of India pursued the policy of giving relief to the business and the banking community at times by

[1] There is no rigid rule according to which the amount of the balance in India and in England is regulated. But it is held that minimum working balance below which the Government does not allow the balances to go is 12 crores in India and £4 millions in England. As in certain months there is a large net withdrawal from the Government treasuries, the Government ordinarily does not budget for a closing balance of less than 18 crores in India and £4 millions in England, or the total of about 24 crores. The actual figures of the closing balances in India and in England show that they have been considerably higher than these amounts. The figures are given below :—

Year.	Closing cash balance in India. Rs.	Closing cash balance. in England. Rs.
1914–15	22,16,90,009	11,86,98,540
1915–16	18,02,40,838	19,20,50,220
1916–17	22,93,98,247	17,08,79,895
1917–18	22,98,77,662	24,93,81,240
1918–19	25,95,03,870	22,07,37,405
1919–20	26,47,59,962	17,99,60,895
1920–21	13,83,56,901	10,81,47,478
1921–22	25,66,13,170	13,49,29,772
1922–23	25,95,80,484	14,73,29,532
1923–24	22,96,85,424	17,70,02,532[1]

[1] (Revised estimates.)

giving temporary loans, but mainly by leaving in deposit with the Presidency banks the proceeds of the loans till actually required and a substantial portion of the balances. The formation of the Imperial Bank has changed the situation for the better by making the cash balances of the Government, to the extent to which they are left with the bank, a part of the general banking balances of the country. But the need of keeping aggregate of the cash balances as low as possible is not less important than before. The balances have during and after the war been quite large. It is not possible to say whether they have been excessive, as the circumstances were quite abnormal. The pre-war figures[1] have in several cases been exceeded, and if they were considered unduly large, the balances of the later years seem to be open to the same criticism. With the growth of the banking and general economic advancement of the country, it should be possible for the Government to manage its finances with reduced balances. The disbursements of the Government have also increased, and will increase still further with the assumption of fresh activities, but in spite of this fact the reduction of balances can and ought to be effected. It is, of course, difficult to lay down any criteria according to which the amount of these balances should be determined from time to time. The actual working of the financial system must be a reliable guide for the purpose. A general maxim, like the one that the Government should neither err on the side of being over cautious, nor take unnecessary risks, is not, like all general maxims of its kind, practically very helpful, and may be taken as a guiding principle for regulating the treasury balances, if the interpretation of what is a right

[1] The figures of the pre-war years which gave rise to the controversy referred to above are given for comparison. They are :—

Year.		Closing cash balance in India.		Closing cash balance in England.
1909–10	....	£12,295,428	....	£12,799,094
1910–11	....	£13,566,922	....	£16,696,990
1911–12	....	£12,279,689	....	£18,390,013
1912–13	....	Rs.28,93,96,967	....	Rs.14,68,44,510
1913–14	....	Rs.23,41,23,799	....	Rs.12,23,65,980

mean between the two extremes is left to the executive authorities.

It has already been stated that these general balances constitute a fund in which there are no compartments. It is an undivided whole. The provincial balances are left with the Government of India. There are no Provincial Government treasuries as distinguished from those of the Central Government. All provincial revenues are paid into the treasuries and all provincial charges paid by them. The unspent provincial balances are, more or less, in the nature of book credits, and the Government of India has the disposal of all the money. The amount which each Provincial Government has got to its credit is shown in the accounts, but it is not kept distinct from other funds. Before the Reforms each Provincial Government had to keep a minimum balance with the Government of India, fixed according to the size of the province, and its liability to famines, and other contingencies of a similar character.[1] Ordinarily the provincial balances were above the prescribed minimum. The Provincial Governments could not draw upon these balances without the previous consent of the Government of India, and their reduction below the minimum was allowed under very exceptional circumstances. The restrictions imposed on the withdrawal of the balances were justified by the double necessity of not disturbing the ways and means position, and guarding against the possibility of a Provincial Government not being able to meet its own liabilities. The rules regarding the maintenance of the minimum balances have now been abrogated in order to give greater financial independence to the provinces. The Provincial Governments now act on their own responsibility in the matter. Except that the Government of India require a timely notice from the Provincial Governments when the latter want to draw upon their balances, they are at liberty to do with them

[1] The prescribed amounts were: Madras, Bombay, Bengal, and United Provinces 20 lacs each; Burma and Bihar and Orissa 12 lacs; Punjab, Central Provinces, and Assam 10 lacs.

what they like. The Government of India can "in the financial interest of India as a whole" require the Provincial Governments to regulate their expenditure in a way as to keep the balances to their credit at a particular figure, or to put it euphemistically, invite them "to co-operate in conserving the financial resources of the State in case of war or similar crisis of first-rate importance." This power is, however, to be used very rarely, and, as a rule, the Provincial Governments can dispose of their balances as they please. If a Provincial Government is debarred from drawing on its balances, the Government of India are liable to pay from the central revenues interest on the amount, which it is not permitted to draw.[1] The changes that have been made are in keeping with the spirit of the Reforms. The financial autonomy of the provinces must carry with it the liberty to spend their accumulated surpluses at their own discretion. The provinces are not allowed to invest balances as they like. They have to leave them with the Government of India, and do not get any interest on them unless they are prevented from withdrawing them. The restrictions regarding the investment of the provincial balances are the result of the policy of keeping all liquid resources of the Government under the central control, and they are not a very great hardship, in view of the fact that each Provincial Government can utilize its surplus funds in developing its own resources. The present arrangements are quite satisfactory in this respect.[2]

[1] Interest is calculated at the average rate at which the Governor-General in Council has borrowed money in the open market during the year by the issue of the treasury bills.

[2] The question of separating the provincial from the central balances has been under consideration, and a tentative scheme formulating general principles of procedure has already been prepared. Mr. Jukes, in his memorandum prepared for the Reforms Enquiry Committee, from which one extract has already been given, puts in a plea for the separation of the provincial balances in the following words:

"It would undoubtedly be a considerable advance in the provincial autonomy if the Local Governments were permitted to assume the custody of their own balances, and freed from all restrictions as regards their drafts upon them, and their procedure in the matter of withdrawal, transfer, and disbursement of provincial moneys. If Devolution Rule 21

It is not enough that the treasury balances should be adequate for making daily disbursements. They have to be distributed among hundreds of treasuries and sub-treasuries. The "Resource Operations" of the Government of India are the machinery by which the treasuries are kept in funds. The beginning of these operations is the framing of these estimates for the ensuing year or pre-

were cancelled, and Rule 16 amended to make the Local Governments custodians of their own 'public account,' important results would follow. In the first place the Local Governments would become responsible for their own ways and means. At present, it is the function of the Central Government to make money available to Provincial Governments at the times and places at which they desire to draw it. If they took over their own balances the Local Governments would have to perform this function for themselves. Indeed it might be possible to let them perform it for the Central Government, in places in which there is no branch of the Imperial Bank. This would involve maintenance by certain of the Local Governments of larger balances than they find necessary at present. On the other hand, the change would give to the Local Governments far larger resources than they enjoy under the existing system. Very considerable sums of money are deposited for short periods with the Government. Among these may be mentioned such deposits as civil and criminal court deposits of various kinds and balances of muncipalities and other local bodies. Sums so deposited are eventually withdrawn, but they represent a large and practically constant balance on the Government account. The majorities of these deposits are in connection with the administration of provincial subjects, but the Local Governments have not hitherto enjoyed the use of them. They do not represent 'revenue' in any sense of the word, and are naturally not classed as sources of provincial revenue. They are funds temporarily deposited in Government balances, and the Central Government as the custodian of those balances and the universal banker, has had the use of them for its own ways and means purposes. If the Local Governments assume the custody of their own balances, they will acquire with it the right to use of that portion of the balance of deposits which has accrued in connection with the administration of the provincial subjects. The sums involved in every case will be far more than sufficient to place the provinces in funds to meet their day-to-day requirements."

Referring to the scheme, which has been prepared for the separation of the provincial balances Mr. Jukes, said:

"It seems probable that the change could be effected without grave administrative inconvenience or serious expense either to the Central or the Local Governments. But a change of this kind must inevitably be accompanied by the separation of accounts from audit, which in itself involves some extra expenditure."

The question of the provincial balances was considered by the Finance Members' Conference, held in November, 1924, at Delhi, and it is reported that some scheme is to be devised by which the Provincial Governments are eventually to have direct dealings with the Imperial Bank, but meanwhile they are to receive some interest on their cash balances with the Central Government, which, as is well known, sometimes run to high figures.

paring what is called the "Resource Forecast." By the end of February each year, each Treasury Officer has to send to the Deputy Controller of Currency, a statement showing what Treasury balances are, in his opinion, required on the last day of each month of the subsequent year. For the purpose of comparison, he gives in this statement figures of the last day of the current and three preceding years. Any variations between the figures of the estimate and the corresponding average of the last four years requires explanation and has to be accounted for. On the basis of this information every Deputy Controller of Currency fixes the normal balances of each treasury in his charge, and intimates to the Treasury Officer the balance for his district on the last day of each month of the coming year. Each Treasury Officer, in his turn, fixes normal balances for his sub-treasuries for each month of the following year on receipt of the intimation of the normal balances fixed for his district. During the course of the year the Treasury Officers have to watch their own balances, and those of the sub-treasuries carefully to see that they do not exceed by any appreciable amount the figures of the forecast. If the actual balances in any treasury or sub-treasury exceed the amount so fixed, prompt steps have to be taken to transfer the excess. It is the essence of the resource work that each treasury should have enough funds to make all Government payments. If the receipts of any treasury are larger than the payments that it has to make, the surplus is transferred to some other treasury, whose own receipts are inadequate for making the disbursements, or to the Imperial Bank which is to keep all the surplus balances of the Government of India. Formerly the funds not required by the treasuries were transferred to the reserve treasuries for custody. Now the Government policy has been changed, and the object of the resource work is to transfer all funds, which are in excess of the amounts needed at the treasuries, to the Imperial Bank to be used by the latter as best as it can, after making due provision for the Government payments,

Each Treasury Officer has, before the third of every month, to submit to the Deputy Controller of Currency an estimate of receipts and expenditure of the current and two succeeding months. The Deputy Controller of Currency can on the basis of this information make a monthly forecast of his cash requirements, and keep sufficient funds at the treasuries and in the Government account of the Imperial Bank for all Government disbursements. The Government takes all precautions against being taken unawares, and it is the duty of the Deputy Controller of Currency to be prepared for all contingencies, which it is humanly possible to foresee as far as the provision and distribution of cash is concerned.

The transfer of funds from one treasury to another and from the treasuries to the Imperial Bank is effected in a manner as to minimize the necessity of cash remittances or the physical transportation of money from one place to another. This is partly done by making use of the bills of exchange, which, as is well known, are used to such a large extent in the national and international trade for the same purpose. But this is also done by the use of another method which is peculiar to this country. The method is quite simple and effective and can best be explained by giving a somewhat lengthy quotation from an official publication in which it is clearly explained. "Under the provisions of the Indian Paper Currency Act the amounts of the notes in circulation may not exceed the amounts of coin, bullion, securities held by the Secretary of State for India or the Government of India. The notes held in the currency chest[1] (which is maintained in almost every treasury and important sub-treasury) are not in circulation, while the coin held in the currency chest is a part of the reserve held by the Government against the notes that are in circulation. Assuming that there are no transactions

[1] The cash in the Paper Currency Reserve is not a part of the Government balances. It is intended for ensuring the encashment of notes. It can be located in any part of India or in England, but cannot ordinarily be used for any other purpose except in exchange for notes, which may be offered for encashment. That is why the cash in the Paper Currency Reserve is kept in separate chests.

elsewhere, the deposit of notes in a currency chest decreases the amount of notes in circulation, or the deposit of rupees in a chest increases the amount of the coin in the Paper Currency Reserve. A deposit of notes or coin in a currency enables the Government to issue notes elsewhere up to the amount of the deposit without exceeding the limits of circulation laid down by the Act. If, therefore, transfer of funds from the treasury balance at A to the treasury balance at B is required, this can be effected at a short notice, and without actual remittance of coin or notes by transferring money from the treasury balance to the currency chest at A, and transferring the same amount from the currency chest to the treasury balance at B. A currency chest thus enables the treasury balance at a treasury or a sub-treasury to be kept at a low figure, as it is possible to replenish the balance quickly by a transfer of money from the currency chest. It also obviates the necessity for frequent remittances of coin and notes, as surplus funds can always be deposited into the treasury chest and made available elsewhere pending a convenient occasion for remittance."[1] The arrangement works very well, and by transfer of cash from the currency chest to the treasury, or *vice versa*, transfer of funds is effected from one treasury to another without any difficulty, the actual remittance of coin or the notes being reduced to the minimum. When a Treasury Officer finds himself in possession of funds considerably in excess of the normal balance he at once deposits the surplus in the currency chest, sending an intimation of his having done so to the Deputy Controller of Currency, who sanctions a corresponding transfer of money from the currency chest to the treasury balance at some other treasury which is asking for funds, or from the currency chest to the public account of the Imperial Bank, thus releasing more money for the use of the latter. The opposite transfer from the currency chest to the treasury can only be made with the previous sanction of the Deputy Controller of Currency, who in according his sanction orders the corresponding transfer

[1] *Vide* Resource Manual, para. 30.

from the balances to the currency chest either at a district treasury or at a local head office or a branch of the Imperial Bank. The object which is kept in view in these transactions is to retain the total amount of the cash in the Paper Currency Reserve of the country unchanged. The district treasury being a unit in the financial administration, the Treasury Officer is responsible for regulating the transfer of funds between the currency chest and the treasury balance within the district. The sub-treasury officer can, at any time, deposit funds from his balance into the currency chest and report the fact to the Treasury Officer, who, without obtaining the previous sanction of the Deputy Controller of Currency, either transfers an equal amount from the district currency chest to the treasury or sanctions a similar transfer at some other sub-treasury in his charge which is short of funds. The transfer has to be made when the sub-treasury officer finds himself in possession of funds in excess of the normal balance laid down for him by the Treasury Officer. A transfer from the currency chest at the sub-treasury cannot be made without the previous permission of the Treasury Officer. The Treasury Officer maintains the balance of the currency chest of the district unchanged, the Deputy Controller of Currency of the area in his jurisdiction, and if the transmission of funds from one province (taking it to mean the total area in charge of a Deputy Controller of Currency, which is different from a province of the civil administration) to another is necessary, it can be brought about by the use of the same device, the Controller of Currency keeping the integrity of the Paper Currency Reserve intact by making the necessary adjustments. This is the ordinary way of transferring cash from one place to another. The use of the bills of exchange is made more with a view to transfer funds from the district treasuries to the more important centres, or afford facilities to the rural centres, than to keep the treasuries in funds, though their use for the latter purpose is not forbidden. The bills of exchange in the official terminology are called the Supply Bills or

Telegraphic Transfers. They are drawn by and on the specified treasuries. The bills are drawn by one Treasury Officer on another on the application of a person who wants to remit money from one place to another. They cannot be drawn for an amount less than Rs.1000, and are drawn in hundreds. The remitter of the money has to pay the cash to the drawing officer, and the payee receives the amount from the Treasury Officer on whom the bill is drawn The Government wants to transfer revenues which are being collected in the treasuries and the sub-treasuries to the provincial head-quarters or other important paying centres, and the merchants want to send money to the rural areas for moving the harvests. Here is the case of what the economists call double coincidence of wants. It suits the merchants and the Government to accommodate each other, the latter coming off better in the transaction[1] by charging premium at the prescribed rates for selling the supply bills. The telegraphic transfers are sold when the remitter cannot afford to wait for the number of the days which will intervene between the payment of the amount by him and the receipt of the supply bill of the payee through the post. He has to pay an extra charge for saving this time. The telegraphic transfers cannot be drawn for less than Rs.5000 and are drawn in thousands. Where the movement of funds from one place to another cannot be effected by exchange between the currency chests and the treasury balances or the issue of supply bills and telegraphic transfers, coins, and notes have to be remitted. It need not be added that when such a necessity arises, great care has to be taken in the despatch and receipt of these remittances.[2] Resource operations are

[1] The Government realized Rs.85,685 in 1922–23 by the sale of the bills. The following charges are made for currency telegraphic transfers and supply bill:

For amounts of Rs.10,000 and more, 1 anna per cent.

For amounts of less than Rs.10,000, 2 annas per cent.

For the telegraphic transfer telegram charges are paid in addition by the person taking the transfer. The telegram charges are Rs.3 or Rs.2, according as the person desires the transfer to be intimated by express or ordinary telegram.

[2] In the year 1921–22 loss on note and specie remittances was only Rs.98.

conducted with very great skill and efficiency. The distribution of funds among the different treasuries requires foresight and promptness in dealing with a rapidly changing course of events. The organization of the Currency Department and the regulations according to which the resource work is done are adequate for achieving this purpose.

The Imperial Bank having taken over the Government receipts and payments, the duty of providing funds at places where there is a branch or a local head office of the Imperial Bank necessarily devolves upon the bank. The Treasury Officer, however, assists the agents of the bank by furnishing him with a statement showing as accurately as possible receipts and disbursements on Government account for the following two weeks, and probable receipts from and remittances to the sub-treasuries. An intimation of an expected payment exceeding Rs.20,000 in one transaction is sent to the agent of the bank by the Treasury Officer as soon as he receives the necessary information. The agent of the bank supplies funds for maintaining the necessary balances at the sub-treasuries, and any surplus accumulating at the sub-treasuries is transmitted to the district treasuries generally through the currency transfer or by actual remittance of notes and coin which are paid into the bank. The rules governing the transfer from or to the chest are the same as those which have to be observed by the Treasury Officers, with this difference, that the sanction for transfer from the currency chest to the balances has to be obtained by the agent through the superior officer of the bank. The presence of the Treasury Officer for all transactions of deposit in and withdrawal from the chest is necessary. For the last three years there has been a progressive decrease of the lock-up of Government funds in the treasuries.[1] This is partly due to the opening of the

[1] Table showing the monthly average of Government balances maintained at the treasuries and the Imperial Bank for the years 1920–21, 1921–22, 1922–23:

Year.	At the Treasuries.	At the Imperial Bank.
1920–21	774 lacs	1267 lacs
1921–22	509 lacs	1391 lacs
1922–23	400 lacs	1895 lacs

new branches. But the more important reason for the change is the opening of a large number of currency chests at the sub-treasuries, their number having risen from 342 in 1920–21 to 892 in 1922–23. It is not necessary, after what has been said in the foregoing paragraph, to explain how an increase in the number of currency chests facilitates the transfer of funds from the sub-treasuries to the headquarters, and their release for the use of the banking and the commercial community. The interlacing of the Government and business finances is inevitable in these days. The existence of the Imperial Bank makes the process more deliberate and purposeful. The resource operations of the Government of India, interesting as they are on account of their complexity and the skill with which they are conducted, are to be looked upon as a survival of the past, whose ultimate elimination can be predicted with a certain amount of confidence. The end is not yet in sight, and the possibility of their complete abolition can even be doubted. They will continue for a long time, and will leave vestiges of their own behind when they cease to count for all practical purposes. But the future line of evolution, unless there is some unexpected deviation, is against their continuance. When the Imperial Bank has developed into a full-fledged State Bank of India, the resource work will become unnecessary. The bank, with its network of numerous branches and with the help of some auxiliary institutions, will regulate the supply of public funds in different parts of the country. The forecast of the balances needed for the ensuing year as a part of the ways and means budget will be necessary, and probably the agents of the bank will continue to need information from time to time regarding the expected receipts and expenditure of the Government. But it will not be necessary for the Controller of Currency and his assistants to have an elaborate machinery for the distribution of funds. The need of maintaining separate currency and treasury chests will also disappear. The issue of the currency notes will become the function of the bank. The paper currency reserve will

be merged into the general cash reserve of the bank, maintained as a backing for the credit liabilities of all kinds, the proportion of the cash reserve to the liabilities being fairly high on account of the importance of securing the absolute controvertibility of notes. The provinces will have their own banking account with this institution, and the only remaining trace of the old dependence of the Provincial Governments on Central Government will also disappear. That this picture of the future is not fanciful will be admitted by those who know what has happened in other countries. It may be a little premature to envisage it just now, but the immediate future can be indicated without inviting that comment. The Imperial Bank will extend its activities and reduce the necessity and volume of the resource work of the Government of India.

The importance of providing funds in England for meeting the liabilities of the Secretary of State and the High Commissioner has already been referred to. The figures of the disbursement in England will give an idea of the amount of funds which have to be laid in London. The means by which the Secretary of State is placed in funds is one point in the estimates of the India Office with regard to which the Government of India have had always the opportunity of having some say. The provision of funds in England is a very important part of the ways and means programme of the Government of India. It forms the subject of a very careful consideration because of the important effect which the action taken by the Government of India has on the rate of exchange between the Indian rupee and the sterling and the amount of circulation in India. It is not necessary to explain in detail the way in which the monetary system of India is affected by the Government policy in the matter of the provision of funds in England. The subject is controversial and has given rise to acute difference of opinion. The different methods by which the Secretary of State gets money for defraying expenditure chargeable to the Indian revenues, may be briefly explained.

Money is needed for meeting the ordinary expenditure on the establishments of the India Office and the High Commissioner, purchase of stores on revenue and capital account, payment of pensions and leave allowances, and the discharge of maturing debts. There are different ways in which funds in the past have been made available for these disbursements. The two least important methods may be mentioned first. One is the remittance of gold from India to England on Government account, and the other is the purchase of bills drawn on London, in India. These two methods have been rarely used.[1] The third method, which comes very handy at times, is analogous to the use of the currency chest for transferring money from one treasury to another in India. The Secretary of State has two reserves in England, which he can always draw upon when he cannot place himself in funds in any other way. There is no restriction as regards the location of the paper currency reserve. A portion of this reserve is kept in England. How this can be done when the essential purpose of the reserve is to use it for giving cash in exchange for notes in circulation in India is a different story, and need not be narrated here. What is of interest for us is that a portion of the paper currency reserve is maintained in England. It is the currency chest of England with this important difference that its contents are not rupees and notes, but gold and securities which can be readily sold for sterling. This portion of the paper currency reserve is used by the Secretary of State in the same way in which the Treasury Officers use the currency chest in India. The

[1] The comparative unimportance of the two methods can be measured by the fact that from 1834 to 1920 out of the total disbursement in England of about £2,000 millions only £2 millions were made available there by the purchase of bills and 20 millions by the remittance of gold.

The purchase of remittances in India has, however, become more important of late as a method of remittance to England. In 1923–24 out of the total remittance of 42·19 millions, 26·75 millions were sent by this method. The purchase is made through the Imperial Bank. It is the opinion of some students of our currency system that this should be the normal way of remitting funds to England. It will not have any disturbing effect on the Exchange Market if the Government makes its purchases at a time when we have a favourable balance of trade and the supply of bills drawn on England is abundant.

Government of India has to deposit funds from the treasury balances into the currency chest at one of their head-quarters in India, and the Secretary of State can, without violating the provisions of the Paper Currency Act, transfer funds from the portion of the paper currency reserve located in England to his treasury balances, and thereby place himself in funds.[1] The reverse process can also be made use of for transferring funds from treasury balances in England to the treasury balances in India. The other reserve, which also can be pressed into service for the same purpose, is called the Gold Standard Reserve. This reserve again has got a history of its own. But it would mean a very great digression if we were to enter into its past history, and trace its development through the various phases of its existence. It will do for our purpose if we take it as a fund which can be drawn upon by the Secretary of State for his own requirements to the extent to which the Government of India earmark gold in the paper currency reserve in India as a part of the gold standard reserve, which can easily be done by deposit of notes and rupees in the currency chests. The gold standard reserve consists mainly of readily saleable securities, and to a very small extent of gold. The Secretary of State can use gold or the sale proceeds of securities for meeting his requirements provided a corresponding transfer is made from the treasury balances in India. The reserve now stands at a little above £·40 millions and the whole of it is located in England. The fourth means by which the Secretary of State can get money is to utilize the proceeds of the loans, which he almost every year raises in England for financing railway and irrigation programme in India. This is an important method which the Secretary of State always depends upon for his ways and means. The portion of loans which is not used by the High Commissioner in purchasing stores for capital requirements of the Government of India is used by the Secretary of State for making his ordinary payments, the Government of India placing an equivalent amount to the credit

[1] In 1923–24 £5·84 millions were provided in this way.

of the undertaking concerned from the treasury balances in India. The last and most important method for sending funds to England is the sale of Council drafts. The sale of the Council drafts, which till 1893 was nothing but a simple and effective means of laying down in England the funds required by the Secretary of State, later on became the central feature of the machinery by which the complicated Indian Currency System was managed till 1919. But that aspect of the question is not of primary importance for understanding the mechanism of remittances from India to England. The Indian Currency System, in the management of which the Council drafts assumed such an important place, has, so far its most distinctive feature of stabilizing the rate of exchange between India and England is concerned, since September, 1920, been in a state of suspended animation. The original function of the Council drafts for transferring funds from India to England for the use of the Secretary of State is still in operation, and more important from our standpoint. The Council drafts are the English variant of the supply bills and telegraphic transfers, the sale of which, as already explained, is a means of transferring Government revenues from the local collecting centres to the provincial head-quarters. The Secretary of State draws these bills on the Government of India, and sells them to the exchange banks, which want to transfer their funds from England to India. They are paid for in sterling in London and cashed in rupees or notes by the Government of India in India. As India has generally to receive more from the foreign countries in consideration of her exports than she has to pay them for her imports, there is always a demand for these Council drafts, unless the unusual contingency of India having to pay more than what is due to her actually occurs. It is important to take note of a difference between the sale of Council drafts and that of the supply bills. The latter are sold in India, have to be paid for and cashed in Indian money. There is no confusion in the Government accounts by their sale, as the amount of money which the Government receives is

the same which it pays, leaving out of account the premium for the time being, the premium which the Government charges for their sale. But the Council drafts have to be paid for in one currency and cashed in another. This brings in another factor into operation over which the Government of India has not been able to exercise a sustained control. The factor, of course, is the rate of exchange. The rate was regulated by the Government of India from 1900 to 1920. It was 1s. 4d. a rupee till August, 1917, when it had to be raised on account of the phenomenal rise in the price of silver. In February, 1920, it stood at 2s. 4d. Of the few months between February and September, 1920, it is not necessary to say much, except that on account of the adoption of the policy recommended by the Currency Committee, the Government of India had to raise the rate of exchange to 2s. 11d., and then, finding it impossible to meet the demand for sterling, which it thereby brought into existence, it surrendered at discretion to the compulsion of the adverse circumstances, and left the rate of exchange to take care of itself. The Government of India is now pursuing what it calls the "waiting" policy and lets the rate of exchange be determined by the blind forces of the market. Regarding the wisdom or otherwise of the attempts of the Government of India to control the rate of exchange, no more need be said except that they have failed and that the rate of exchange has, in spite of them, been running its erratic course. The fluctuations in the rate of exchange introduces an element of uncertainty in the Indian finances, as the amount of money that has to be provided in India to meet the requirements of the Secretary of State depends upon the rate of exchange. For the purpose of accounts a certain arbitrary rate of exchange has to be assumed, any variations from which of the actual rate means either gains or losses by exchange, which have in the past been considerable. The Indian finances have since 1873, the year in which the silver, the mainstay of the Indian Currency, began to fall in value in terms of gold, have been managed under the

malignant influence of the varying rate of exchange; and it is not known when it will be possible to eliminate its disturbing effect. The advice regarding the reduction of the sterling commitments of the Government of India has been consistently given and as consistently ignored. The solution of the difficulty depends upon a number of important issues, in the settlement of which considerations other than financial have also to be taken into account. In the past the desire to establish a stable rate of exchange has been the dominating factor of the Government currency policy, and given to it a turn which has had many undesirable effects. As the study of our currency system is not within the scope of this book, these aspects of the question need not be considered here. It is enough to take note of the bearing of the varying rate of exchange on the ways and means position and resource operations of the Government of India; and the bearing is that the Finance Member of the Government has every year to plead his inability to forecast the rate of exchange in the ensuing year, and make any definite statement regarding the methods by which the Secretary of State will draw money necessary to meet the sterling obligations of the Government of India. The inference that the situation needs improvement, is too obvious to need an explicit statement. It is unfortunately easier to state the conclusion than suggest the means by which it can be made effective.[1] About the treasury balances of the Secretary of State it is necessary

[1] There is one method by which the Secretary of State gets the funds that he needs for making disbursements which has not been mentioned in the text on account of its spasmodic character. The Government of India has, in some cases, to advance money for expenditure incurred in India on behalf of the Imperial Government which has to be repaid by the latter. The Government of India has to find rupees in India and the Imperial Government pays their sterling equivalent to the Secretary of State. During the war large amounts were received by the Secretary of State in England in this way on account or repayment by the War Office of the amounts spent in India for the expeditionary forces and other war services. From 1914 to 1922, about £228 millions were received by the Secretary of State in this way. This method is still used to a small extent even now. The Government of India has, during 1923–24, paid 2 crores on account of the Iraq Administration which has been repaid to the Secretary of State.

to add a few words. The balances are necessary for the same reason for which it is necessary to maintain them in India, viz. to safeguard the solvency of the Government of India. The problem of maintaining balances in England is not as difficult as it is in India, as the resources of the money market in London are more than adequate for getting over any temporary difficulty that may be experienced in finding the ways and means. The normal working balances in England for which the Government of India makes provision is £·4 millions. A glance at the figures of the last ten years shows that the balances actually located in London have been much higher than the normal figure. For this state of affairs there can be no justification. This part of the argument may be concluded with a quotation from Mr. Keynes, who is not an unsympathetic critic of the policy of the Government of India. He says, "If the Government of India holds in London a penny more than is required for the stability of their financial system, they are certainly diverting resources from India, where they are greatly required, to the detriment of India's trade." The consideration is conclusive for our purpose, and the burden of proof that the sums kept in London were actually necessary for the stability of their financial system lies on the Government of India.[1]

[1] In this connection it is of some interest to give an extract from the evidence of Mr. Abrahams, the late Financial Secretary of the India Office, before the Chamberlain Commission in which he explained the Government policy regarding the transfer of funds from India to England:

"*Q.* (80).—As regards the division of balances between India and England, what determines the amount of balance which is kept in India, I mean, the proportion of the balance? *A.*—The Secretary of State in making his budget, which involves among other things drawing of funds from India, says to the Government of India: 'How much can you spare? because you could not dream of drawing from India more than Government of India can spare, but I fancy, of late, the Government of India have and very wisely, raised their requirements. . . . Nowadays the Government of India says to the Secretary of State, you must leave us a closing balance of 12 millions or thereabouts,' and the Secretary of State has always accepted that, and it is the sort of thing he would never question.

Q. (81).—Speaking generally, do I understand that you keep in India what the Government of India considers a minimum reasonable balance? *A.*—I do not know whether a minimum reasonable quite hits off. I would say reasonable balance. I would not think it right, if I may use

The financial duties described in this chapter are performed by the Controller of Currency. The organization of the Currency Department, of which the Controller of Currency is the head, may be briefly explained here. There are, besides the Controller of Currency, five deputy Controllers of Currency, and seven Currency Officers. In Madras and Burma, the Accountants-General are the *ex officio* Deputy Controllers of Currency. The Currency Officer is in immediate charge of the office of issue of the currency notes. They also play a subordinate part in the movement of funds. Every year the Controller of Currency issues an interesting report on the operations of the Currency Department and the resource operations of the Government of India. The Report, besides giving information regarding the circulation of notes, composition of the paper currency reserve, and other matters connected with the issue of the currency notes and coins, contains very useful information about the ways and means transactions and movement of funds during the year to which it relates. The Report is a very valuable document and ought to be read by those who want to understand the working of our financial system in respect of matters which are brought under review in this publication.

that expression, to cut the Government of India to the bone—to bring down the balance to such an extent that there might be a danger of inconvenience to them. I should say reasonable balance instead of reasonable minimum balance.

Q. (82).—Substantially you keep as much of balance as you can in London? *A.*—No; we do not keep as much of balance as we can in London. That really is an important distinction. We bring to London as much as we can without inconvenience to the Government of India, not in order to keep it there, but in order to spend it there, and I think that you will see that it is very important to distinguish between the two. Supposing that in certain years the Secretary of State decided that he could, bring £2 millions more money than someone else thought he might bring, the effect of his doing, if he conducts his affairs in the way in which the Secretaries of State do, would not be that in the end of the year he would end with £2 millions more money, but probably he would end the year with having borrowed £2 millions less for new railways or having paid off his £2 millions of temporary debt or something of that sort. I am very anxious if he may say so, more especially in view of a good deal misunderstanding that has arisen, to emphasize the difference between bringing as much as the Government of India can spare and keeping in London as much as they can spare."

CHAPTER X

PUBLIC ACCOUNTS

For the orderly conduct of the finances of a nation a sound system of public accounting is absolutely essential. The Indian system of the public accounts is maintained on "cash" as distinguished from "accrual" basis. The difference between the two is that while the former takes the actual receipts and payments as the basis of the account keeping, the latter is concerned with bringing to account the claims accrued and the liabilities incurred. The account officers in India do not take credit for a receipt which though it has fallen due in a particular year, has not been actually paid in it, and do not show a charge as having been incurred unless money in payment thereof has actually been issued from the Treasury. The pay and allowances of the public servants, for example, for the month of March, which are paid in the beginning of April, are included in the accounts of the fiscal year in which they are paid, and not the year in which they are earned. The arrears of the Income-tax, and other taxes, which are not paid in the year in which they fall due, are credited to the account of the year in which they are actually received. The budget estimates are framed on the basis of what is expected to be received and paid during the following year, including the arrears of the past year; and in the accounts sums paid in and paid out, irrespective of the period to which the claims and the liabilities belong, are shown as receipts and expenditure. When we speak of income of a particular year, we mean the public revenues which have been collected during that period and not the dues which, properly speaking, ought to have been paid in it; and similarly the public expenditure of a year is the sum total

of the amounts which have been paid to the creditors of the State, even though the liabilities for which the payments have been made were incurred in the previous years. In France and some other European countries a different system is followed. There, "every liability is brought into the accounts for the year which has been incurred therein, although no payment is made for it till long after, and similarly revenue is brought to account that ought to have been received, although it may not have been received in fact."[1] The chief merit of the latter system is its accuracy. It, to use the words of Bastable, invests the fiscal year with a personality, and is the truthful record of the income and expenditure of the year. It is not possible under this system for an officer, who has exceeded his sanctioned grant, to hold over the payment of a particular amount for a few months, and debit it against his grant of the next year; and we can know the real yield of different taxes during a particular fiscal period, though the realized amount may be a little smaller. A business corporation, which adopts the cash account as the basis of its financial operations, can give a very misleading account of its real financial standing. The conclusion as regards its being a paying concern depends upon the comparison of its earnings and expenses, and not its payments in and payments out. Cash in hand of a business firm is not a criterion of its financial soundness. Surplus or deficit of the Government, which is the result of putting the amount received against the amounts paid does not show whether it has been able to balance the income and expenditure of the year. But in spite of its manifest disadvantages the system of cash accounts has some merits of its own, which account for its adoption in England, the United States, America and some other leading countries of the world. There the accounts of the fiscal year are closed on the last day of the year; all the outstanding amounts, whether due to or by the State, are carried to the accounts of the next year, and all appropriations not used are annulled.

[1] *Vide* E. Hilton Young, "The System of National Finance," Second Edition, page 179.

The promptness with which the accounts are closed and the financial position of the Government exhibited is the main recommendation of the system. Every year a new beginning can be made, and the public, within a few weeks of the expiry of the year, can ascertain the state of the nation's financial affairs. In India, on account of the fact that the budget is presented to the Legislature a month before the commencement of the fiscal year, the actual figures of receipt and expenditure do not receive any public attention. The figures shown in the revised estimates, which, as already stated, are composed of the actuals of eight or nine months and estimated ones of three or four, are taken as the basis of comparison with the budget estimates and made the subject of public comment and discussion. But the total receipts and expenditure of the last year can be known in about the third week in April. So far as the ordinary activities of the Government are concerned, no serious objection can be urged against the system of cash account. If sufficient precautions are taken against its abuse by the officers who want to evade the rule regarding strict adherence to the scheme of appropriations, the practice of bringing to account all receipts and expenditure of the year, though they do not belong to it, has the advantage of simplicity and obviates delay in balancing accounts. When we take into account the variety and complexity of the financial operations of the Government, these advantages constitute a great recommendation of the system. But the Government of India has, besides these activities with regard to which liabilities and assets are a matter of no consequence, undertaken quasi-commercial activities like railways and irrigation, which are expected to yield a reasonable rate of profit. In their case it is desirable to know how much they have earned during the year and how much has been spent on them. This cannot be done if the accounts of these departments are also maintained on the cash basis. For the sake of uniformity and promptness their accounts may also be closed with the accounts of the other public departments,

but if their real income and expenditure, apart from their actual receipts and payments, have to be ascertained, it is also necessary to compile their accounts on the basis of the accrued assets and accrued liabilities. In the matter of classification, as remarked a little later, a distinction is made in their case, and all charges which are incurred on their account are debited against them, though they may be paid by other departments. In the matter of accounts also it is a matter of importance to exhibit the real financial standing of these undertakings, and set the amounts due by against the amount due to them and thus arrive at a correct appreciation of the financial results of their operations. With this reservation no exception can be taken to the underlying principle of the system of public accounts in India. It is built upon the basis of the accomplished facts, enables the Government and the public to know the state of the public finances without undue delay, and makes it easy to strike a balance of accounts by cutting off sharp the record of financial transactions on the 31st March every year.

The second characteristic of the system of the public accounts in India is the close correspondence between the form in which the estimates are framed and that in which the financial transactions are posted in the account books. The reason for this similarity is obvious. Without this it would be impossible to compare the budget estimates with the actual receipts and expenditure, and see how far the anticipations have come true. It is necessary for framing the budget estimates every year to take into account the figures of the previous years and make forecasts on their basis, of course, making a due allowance for the variations which a knowledge of tendencies likely to affect the financial proceedings of the ensuing year, may suggest. But the most important reason for this feature of the system of public accounts is that it makes the enforcement of the scheme of appropriations easy and the financial control of the spending departments effective in practice. Each spending officer has got his own assignment. This limit he, in ordinary circumstances, is not to exceed. It is

easy for him to know the rate of the progress of the expenditure and judge the possibility of his meeting the obligations within the sanctioned amount, if the main divisions and the sub-divisions under which the charges are brought to account are the same as those under which the figures in the budget estimates were arranged for the sanction of the Legislature and the Government. He can watch the rate at which the expenditure is proceeding, and in case he anticipates any excess, apply for additional funds in time to the authority competent to grant them. The accounts officer, on the other hand, can compare the actual expenditure with the appropriations, and if in his view excesses appear to be likely, he can, and has, to issue warning to the spending officers to enable the latter to ask for extra funds in time from the competent authority. This cannot be done if the money is granted under certain specified heads, and the expenditure is accounted for under other and dissimilar heads of account. It is, therefore, necessary to make the units of appropriation and grants correspond to different heads of account under which individual items of expenditure are recorded. It was pointed out in Chapter III that the figures in the Books of Estimates are arranged according to the needs of the units of administrative organization. The Legislature and the Government grant money for the expenditure of different public departments, and not for the purposes for which it will be incurred, except in so far as particular departments have special functions of their own, and therefore fulfil special purposes. In order to establish a correspondence between the form in which the estimates are framed and that in which the accounts are kept, it is necessary to adopt the same principle in public accounting. In classifying expenditure or taking it to the head of account to which it belongs, the object kept in view is to debit it against the department which spends the money and not the purpose for which it is spent. To put it technically, the basis of classification is subjective and not objective. This method has a disadvantage of its own. It makes a little difficult to know

the amounts which the Government is spending for different public activities. If we want to know the amount which the Government is spending on national defence, preservation of peace and order, diffusion of education, promotion of sanitation, or development of commerce and industry, it requires a certain amount of effort to collect the information from the accounts of the Government. In many cases the Government departments engage in a number of specific activities in performing their public duties. The district officer and his staff, as is well known, are responsible for the performance of many functions. The district officers collect land revenue, administer justice, maintain peace and order, manage the working of treasuries, and supervise the administration of other public departments and in some cases of the local bodies. It is almost impossible to split the total expenditure on district administration into as many parts as there are activities entrusted to district authorities, and ascertain the amount spent on each activity. The distribution, if effected, cannot but be more or less arbitrary. The total amount spent by the Government on the promotion of commerce and industry is accounted for under many heads. To give an instance, the expenditure incurred for supplying commercial and industrial information is borne by the Statistics Department and the expenditure incurred in running the pioneer factories, or giving subsidies to private firms is charged to the Department of Industry. The incidence of expenditure on stragetic railways, which are primarily maintained for military purposes is also determined subjectively. The amount is charged to Railways and has the effect of exaggerating their working expenses and reducing their profits. The Public Works and the Stationery Departments exist for the benefit of all other departments. The expenditure incurred by them, if it was to be classified according to the different activities, would have to be distributed among the different departments for the benefit of which they exist. But, as it is, the total expenditure of these departments is debited to their

account and no attempt is made to distribute it according to the purposes for which it is spent. The illustrations could be multiplied, but enough has been said to show how the subjective principle of classification is, from this standpoint, a source of confusion. It is more important for the man in the street to know how the total public income is being spent, what is the proportion of expenditure for various purposes, and how far it is in accordance with the relative importance of the specific public activities. Why, then, is this principle adopted ? The arguments in its favour are two, and from the point of view from which they are urged, conclusive. The one is that it is necessary to classify expenditure on this principle as without it due stress cannot be laid on the factor of personal responsibility. In the administration of public departments the individual officers are in charge of the divisions and sub-divisions of the Government and not of the different categories of work. This being so, each officer is responsible for spending money on the particular unit of organization of which he is in charge. They have to estimate the needs of the services placed under their direction, and after the budget has been sanctioned to watch their expenditure. It will not do to break up and scatter the estimates of each individual officer in different parts of the estimates, and call upon him to control the administration of a grant, when the expenditure is being incurred by two or three departments, which are practically co-ordinate for the purpose of public administration. The other and less important reason for having a subjective basis of classification is that the estimates and the accounts give a picture of the structure of the Government and show the amounts which are to be or have been spent for maintaining a particular division or sub-division of the Government organization. This general rule regarding the incidence of public charges does not of course rule out the possibility of collecting information regarding amounts spent for specific activities. Such information can be and is collected to know how much money is being spent for different purposes.

There are two important exceptions to the subjective principle of classification. The Reforms have introduced a complete separation of the Central and the Provincial finances. As a natural corollary of the separation of the finances, the accounts of the Central and Provincial Governments have also been separated. The receipts and expenditure of the Central and the Provincial Governments are credited and charged to the accounts of the Government concerned, irrespective of the departments by which they are realized or paid. The expenses of the salary and the establishment of the High Commissioner are chargeable to the central revenues, but he purchases stores for and makes payments on behalf of the Provincial Governments. All such charges are passed on by him to the account of the Provincial Governments and are met out of the provincial revenues. The various departments under the administrative control of the Provincial Governments are performing the agency functions for the Central Government. When these services are maintained exclusively for the administration of a central subject, the entire cost of its maintenance is charged to the account of the Central Government, and when they are employed for joint work their cost is shared between the Central and the Provincial Governments on some agreed basis. The other exception to the general rule is that revenue and expenditure of the Railways, Post and Telegraph, and other commercial departments are accounted for separately in order to know their earnings and expenses. In their case the basis of classification is objective. The adoption of this basis is necessary to ascertain their financial standing and find out whether they, as business corporations, are paying concerns. To give a concrete instance, the railway audit officers are not railway employees in the ordinary sense of the word. They are officers of the Central Government and perform their duties under the supervision of the Finance Department and the Auditor-General, but the expenses on account of their salaries and establishment are charged to the receipts of the railways, whose accounts they audit, the idea being

that each railway should meet its audit expenses from its own revenues. The charges incurred for the purchase of railway stores are passed on to the railway concerned and any receipts and payments by the commercial departments for one another have to be duly adjusted between them. But with these exceptions the general rule holds good that the "classification in public accounts has closer reference to the department in which the revenue and expenditure occurs, than to the object of revenue and expenditure or the grounds on which it has been sanctioned."[1]

Very great care is taken to secure a uniformity of accounts in spite of the volume and variety of the financial transactions of the Government. The Auditor-General is the principal authority for determining the form of accounts, and no important change can be made without his sanction. The heads of classification are the same for all spending authorities. The accounts of the Secretary of State, High Commissioner, the Central Government, and the Provincial Governments are maintained on the same basis. It is not necessary to point out the advantage of uniformity. The principles of public accounting do not admit of any variations. They are the same for all administrative authorities. This uniformity in the system of public accounts makes the comparison of the accounts of different authorities and times possible, and is a great help in the formulation of the general principles of the financial administration. If the spending officers are given discretion in changing the form in which the accounts are to be kept and rendered by them, it will, besides introducing confusion in the financial administration, make it impossible for the central authority to present a record of the financial transactions of the country as a whole, and vitiate the value of comparing the financial results of the

[1] The Esher Committee recommended that for the military expenditure should be instituted what are called "block votes"—that is the accounts should record the whole expenditure of each class of units and formation including the cost of stores but excluding the accommodation. The principle has now been adopted and all charges are now allocated to the service for which they are incurred with the exception of certain charges like the Military Works, which are recorded separately.

different units of administration and different periods. It was pointed out in Chapter III that the frequent changes in the form of estimates makes their study unnecessarily embarrassing. What is true of the form of estimates is also true of the form of accounts. It is worth while repeating that the estimates and the accounts are closely bound up together, and though the changes have been made in their form in the past and will have to be made in the future, their introduction requires a mature consideration and expert handling. The duty which has been laid on the Auditor-General according to the rules framed under Section 96D of the Government of India Act, is a very important part of his work. When and if the audit and account functions are ultimately separated, the Auditor-General will be relieved of his duties with regard to the accounts, and the work of prescribing the form of accounts will devolve upon the Finance Departments. But even then it will be necessary for the Finance Department of the Government of India to exercise a certain amount of control over the form of the accounts in the interest of uniformity and co-ordination.[1] The general framework of accounts should be the same throughout the country.

The uniformity of accounts is the legacy of the centralization of finances and consequently centralization of accounts. The centralization of finances has, to a con-

[1] The British Treasury lays down the form of the estimates and the accounts, and is responsible for ensuring correspondence between the two. The Finance Departments in India are responsible for preparing the estimates and incidentally determining their form, while the form in which the accounts are to be maintained is under the control of the Auditor-General. At present the estimates are prepared under the same heads under which the expenditure is recorded. That is as it should be. But the fact that the form of the estimates is to be determined by one authority and the form of accounts by another and independent authority is wrong in principle. There is no possibility of the forms of the estimates and the accounts showing any material divergence from each other, so long as the Accountants-General are associated with work of the preparation of the estimates as closely as they are at present. But when the audit and the accounts duties are separated, as it is suggested that they should be, it would be right and proper to make the Finance Department responsible for both the form of estimates and the accounts.

siderable extent, been replaced by decentralization, and the centralization of accounts still remains and will continue as long as further constitutional changes are not effected. Broadly speaking the transactions in the public accounts fall in four groups: revenue, expenditure, debt, and remittance. The first head does not call for any explanation. To it are credited all receipts of the Government derived from taxes, commercial departments, and other sources of income. The second group is made up of two parts, one representing the expenditure charged to revenue, and the other the expenditure met mainly from the borrowed funds. The comparison of revenue and the expenditure charged to revenue represents the surplus and deficit of the Government. The expenditure from borrowed funds is usually of a remunerative character (productive in the sense already explained) though not inconsiderable amounts are spent on works of public utility like the construction of New Delhi and Bombay Development Scheme, which are not directly remunerative. The expenditure charged to revenue also includes capital expenditure, but the amounts so spent are, comparatively speaking, unimportant. The third division comprises all transactions with regard to which the Government acts as a banker, lender, or borrower. The receipts under this head constitute liabilities and payments assets, together with the repayments of the former or the recovery of the latter. All receipts and disbursements on account of loans, departmental or judicial deposits or advances made by the Central and the Provincial Governments appear under this division. The fourth and the last division represents what are called the adjusting heads, under which appear all transactions connected with remittance of cash and the amounts of receipts and payments, the credit or the debit for which has to be passed on to the Government or the department on whose behalf the receipt is realized or the payment made. The latter transactions are technically called the transfer adjustments and occur between India and England, between the provinces or the depart-

ments dealing with different accounts officers. The transactions are provisionally entered under the broad division "Remittance" and are cleared eventually by adjustment under the final head, to which they properly belong. They do not affect the totals of receipts and disbursements of the Government, which are collectively represented by the first three divisions, and are merely book entries for the purpose of accurate account keeping. These four divisions are divided into sections under each of which are grouped receipts and charges of cognate character. They are distinguished by the letters of the alphabet, double letters representing the capital transactions. For example, railway transactions, both of Revenue and Expenditure, are represented by the letter B, and capital expenditure on railways is represented by BB. The Revenue and Expenditure sections are further sub-divided into major heads which are units of classification in public accounts. The major heads are numbered serially, the Roman numerals being used on the receipt side and the Arabic on disbursement side. Section A deals with principal sources of central and the provincial revenues, and charges in respect of collection and administration thereof, the revenue earned by the commercial departments being dealt with in separate sections assigned to those departments. The major heads under Section A are Customs, Income-tax, Salt, Opium, etc. The receipts from the Customs duties are denoted by the Roman numeral (I) and the expenditure for their collection and administration of the Customs Department by the corresponding numeral (1). To give another instance, Section K stands for Military Services and comprises three major heads, Army, Marine, and Military Works. These three major heads are represented by the numerals XXXVI, 48; XXXVII, 49; XXXVIII, 50; respectively. Debt and Remittance divisions are not divided into major heads. Major heads are given sub-divided into minor heads, which are in their turn split up into subordinate heads called detailed heads. The sections and the major heads are

given in the Appendix (VI).[1] Running across these divisions and sub-divisions of accounts there is the differentiation of receipts and disbursements into central and provincial, of expenditure into voted and non-voted, and of provincial expenditure only into reserved and transferred. These divisions are necessary in order to establish a correspondence between the system of public accounts and the scheme of public finance, which is organically connected with the administrative machinery set up by the Reforms. The receipts and disbursements of the Government are classified with minute elaboration. The accounts when consolidated give a comprehensive and exact idea of all financial transactions which go to make up the total receipts and disbursements of the Government. The detailed heads are combined into minor heads, minor into major heads which are grouped into sections and are ultimately brought together into three main divisions (leaving out remittance for reason given above). Whether we proceed from top downwards or bottom upwards, we can get through the accounts a complete insight into the financial machinery of the country. Without the system of detailed classification it would be impossible to secure regularity in financial transactions, and regularity is the essence of all good account keeping.

Capital expenditure has been referred to a number of times in the foregoing paragraphs. It is important the allocation of expenditure between revenue and capital account should be correctly made. In the case of the commercial departments it is obviously very essential to classify expenditure on a scientific basis. To know whether a business corporation has been a success from the financial point of view, one has to see whether it can meet its expenditure from its income without in any way impairing

[1] There are twenty-four major heads of receipt and sixty of expenditure, the minor heads run into hundreds, and detailed heads into thousands. In respect of major and minor heads the prescribed classification has to be strictly observed ; but with regard to the detailed heads, the Accountants-General have wider discretion, though unnecessary multiplication of these heads is to be avoided, and a new head opened when it is absolutely necessary.

its permanent equipment and yield a certain rate of profit on the amount invested in the concern. If it cannot do that, it is evidently, as phrase goes, living on its capital, which course, if persisted in, is likely to lead to the ultimate ruin of the business. The Government in India has undertaken a number of business enterprises. The motive for doing so has not been purely economic, that is they have not been undertaken with a view to increase its income, but have nevertheless to be managed on a commercial basis. The working expenses of these departments, which include the expenses for running them as going concerns, keeping them in a state of good repairs, and providing for the renewal of the plant when it wears out, have to be deducted from their gross revenue in order to arrive at their net contribution to the yearly income of the State. For this purpose it is necessary to maintain a separate account of the amount spent on the concern for enabling it to perform its proper function and charge to it all expenditure which improves its earning capacity. Whether a particular item of expenditure should or should not be charged to this account does not depend upon the source from which the funds are provided. The bulk of the expenditure has in the past and is still met out of the funds borrowed in the market or the saving bank deposits, which practically comes to the same thing, but a small portion of this expenditure is also met out of the ordinary revenues. The real test for determining the incidence of a charge, as far as its allocation between the two accounts is concerned, is its effect on the revenue-yielding capacity of the department. If the expenditure improves its equipment, or otherwise makes it possible for it to render service in a more efficient manner, it is chargeable to capital account. If, on the other hand, it keeps the present equipment intact, or prevents its deterioration, it should be considered a charge on the earnings of the department. The application of this general principle is not a simple affair in actual practice. It is very difficult at times to differentiate a transaction from this point of view. The expenditure at times appears

to have been incurred for replacing the old worn-out equipment, while it actually places the business as a whole on a better footing. As often it is possible to give specious reasons for charging expenditure to capital account, which, properly speaking, should be met out of the earnings of the department. The allocation of expenditure between revenue and capital account, therefore, requires special care and attention. In all commercial departments it is necessary for the proper maintenance of their accounts that this point should receive special consideration, but in the case of railways, managed by the companies and owned by the State, it is of particular importance. The dividends of these companies depend upon the net earnings of the railways, which can be artificially inflated by charging revenue expenditure to capital funds.[1] Special rules have been prescribed in the case of these companies to secure the proper classification of the charges, and it is the duty of the audit officers to secure their observance.[2] In the discharge of this important duty the element of personal equation has to be taken into account, as it requires the exercise of discrimination—a quality the exercise of which cannot be regulated by any rule of thumb. It is, however, necessary to bear in mind that the determination of what is capital expenditure is of very great importance in the system of public accounts in India.

Having explained the general principles on which the public accounts are kept in India, it is worth while to trace the different stages through which they pass, and see how they are built up. In the case of the Civil and the

[1] During the war on account of the inability of the railway authorities to get the materials from the manufacturing firms, the railways in India were allowed to fall into a state of bad repairs. The proper course would have been to set apart the amounts which could not, on account of the war conditions, be spent on the maintenance of the railways and constitute them into a replacement fund to be used later for making up the arrears. But instead of following that course the Government allowed the sum which could be employed for the upkeep of the railways to be shared between the companies and the public treasury, with the result that it increased the contributions of the railways to the public revenues and also the dividends of the companies and left a legacy of arrears, which it will require time and special efforts to make up.

[2] *Vide* Appendix VII.

Public Works Departments, their transactions are, in the first instance, roughly classified by the treasuries according to their major heads, all doubtful ones being lumped together under the nondescript heading "miscellaneous." The documents which the district treasuries forward every month to the Accountant-General in support of their accounts of receipts and payment are thus classified. In the case of the departments which draw funds on their letters-of-credit, this is done by their disbursing officers before they submit their accounts to the audit officers. These are initial accounts—the primary fabric out of which the texture of the month's account is woven. The second stage in the process is the classification of each document of receipt and payment in minute details in the account offices. Major heads given on them have to be checked and the minor and the detailed heads, to which the transaction belongs, written on the vouchers. As there are hundreds of minor heads and the detailed heads run into thousands, the specification of vouchers according to heads and the subheads of accounts has to be done with very great care. After these items have been classified the next stage is to bring all these items pertaining to every head of account together, and total up the expenditure incurred under each head—technically called the compilation. The accounts of the whole circle in charge of each officer are thus compiled month by month; the receipts and expenditure of the whole province, or each account division in case of the departments which have their accounts offices, are grouped and totalled and the actuals compared with the sanctioned estimates. Warning which is issued to the spending officers by the account officers when the rate of expenditure makes the excesses above the budget provisions likely, is the result of this comparison. The work of classification and compilation is rendered more complex on account of the necessity of grouping receipts according as they are central or provincial, and expenditure under voted and non-voted heads and provincial expenditure under two additional heads, transferred and reserved, for there are

voted and non-voted heads of expenditure, both in the reserved and the transferred departments and the same head of account is both transferred and reserved, voted and non-voted. The grouping is made as under :—

Revenue.	*Expenditure.*		
Central.	Central :	Voted.	
		Non-voted.	
Provincial.	Provincial :	Reserved :	Voted.
			Non-voted.
		Transferred :	Voted.
			Non-voted.

On the first of the month succeeding that to which the accounts relate an extract from the abstract of receipts and expenditure known as the Civil Accounts showing the receipts and expenditure under major heads, in which are also included lump-sum receipts from and issues to military and other departments, are sent to the Controller of Currency, who consolidates them and compiles an abstract for the whole country and forwards it to the Finance Department of the Government of India in the third week of the same month. He also receives and forwards to the Finance Department the accounts of Railways and Posts and Telegraphs, classified according to major heads, a few weeks later. After the close of the year the civil and the departmental Accountants-General prepare classified accounts of the transactions which they are in charge of, and submit them to the Auditor-General who consolidates them together into "Finance and Revenue Accounts" of the Government of India in the form prescribed by the Secretary of State for submission to the latter. The Finance and Revenue Accounts are the authentic record of the financial transactions of the Government for the whole year. At the end of every month the Accountants-General prepare from the joint accounts of the Central and the Provincial Governments abstracts of the monthly accounts of the Provincial Governments showing the state

of provincial receipts, expenditure, and cash balances for their information. It has already been stated that nomenclature of the major and minor heads and their order is uniform in all account offices. It is on account of this uniformity, possible to prepare an all-embracing account of the Government, on the basis of which an intelligent and well-informed judgment on the financial operations of the year can be formed. The need of uniformity, which was emphasized above becomes patent, when we realize that, but for it, it would not be possible to take a comprehensive view of the financial operations of the Government as a whole.

The accounts of the Secretary of State are prepared by the Accountant-General of the India Office and those of the High Commissioner by his Chief Accounting Officer. The Indian accounts being maintained on a rupee basis, the figures given in the Home accounts which are necessarily expressed in sterling, the English money, the rate of exchange at which they are converted into rupees introduces another complication in the Indian accounts. The rate of exchange has since 1917, as already stated, been fluctuating. In these days the official rate, at which the accounts are kept is 2s., but as the market rate which determines the amount of rupees charged in the Indian accounts on account of transactions in England has been, taking the average of the last three years, about 1s. 4d.,[1] there has been arising considerable loss on account of the lower rate of exchange, the amount of loss being measured by the difference between the number of rupees required to meet the sterling charge at 2s. to the rupee and number of rupees actually required to make the payment. This amount was formerly shown as a lump sum against the general heading exchange, but since the financial year 1923–24 the loss on account of exchange is separately entered against each head of account, and in order to get an idea of the total loss on this account, the amounts

[1] The average rate for 1923–24 was 1s. 4½d. and the assumed rate for 1924–25 is 1s. 4⅞d.

scattered under the different heads of account have to be brought together and totalled up.[1] This feature of the Indian accounts will continue to produce its confusing effect as long as our monetary system is experimented with either in empirical or scientific manner. It is wrong to tamper with the basis of economic life—the standard money—merely to steady our public finances, but if a sound system of currency can be introduced, which besides being suited to the economic conditions of India, will incidently eliminate the variations of exchange, it will remove an important speculative element in our estimates and accounts—a consummation to be devoutly wished for on account of the existence of other elements of uncertainty in Indian finances.

The audit and account functions in India are performed by the same officer. The question of their separation is one of those questions which have been raised a number of times, but which, to use the language of ordinary parlance, is still hanging fire. The organization of the Audit Department will be explained in the next chapter, and this question will, in that connection, be discussed at some length. But it has to be borne in mind that in this book, when the audit and account officers are mentioned, reference is to the identical officers. There is, however, another question connected with the bigger question of the separation of the audit and account functions, which is of some importance and may be briefly dealt with here. The Accountants-General are responsible for maintaining the

[1] The procedure for the allocation of exchange losses is as follows: All exchange losses arising in respect of exchange transactions are recorded in the first instance provisionally under what is technically called the suspense head "Exchange and Remittance Account," the portion attributable to revenue and capital accounts in respect of outlays incurred in England is calculated every month on the basis of the average of daily telegraphic transfers rates from Calcutta to London and transferred to these accounts and the portion relating to the expenditure of the Provincial Governments is similarly debited to the Provincial Governments concerned by necessary adjustment. The effect of these adjustments is that the losses by exchange are distributed over the respective heads of revenue and expenditure. In 1923–24 14·98 crores have been debited to various heads on account of the difference between 2s., the official rate, and 1s. 4½d., the average rate for the same year.

provincial accounts. They are officers of the Central Government and are under the administrative control of the Finance Department. They are expected to render assistance to the Provincial Governments in all financial matters, but are not amenable to their discipline. In the event of the separation of the audit and account functions, it will be advisable to change the position of the accounts officers and make them officers of the Provincial Government. The duty of keeping accounts is an executive function, and with the devolution of the independent financial authority on the Provincial Governments, it is inconsistent to allow the officers charged with its performance to remain outside the control of the Provincial Governments. The accounts being a statistical presentation of facts, a complete separation of the provincial from the central finances should be reflected in the separation of the provincial from the central accounts. A certain amount of central regulation will be necessary to secure a uniformity of general principles in the structure of the accounts. But the officer responsible for the maintenance of provincial accounts should not retain any supervisory function in matters of provincial finance. They should be under the complete control of the Provincial Finance Departments.[1]

[1] The view expressed in this paragraph is supported by the testimony of Mr. Jukes, an extract from whose evidence before the Reforms Enquiry Committee is given at the end of Chapter XI.

CHAPTER XI

AUDIT OF PUBLIC ACCOUNTS

The financial operations of the Government are carried on a somewhat cynical assumption that in matters relating to public money no one can be trusted. This assumption leads to the introduction of an elaborate system of checks and rechecks, without which, the human nature being what it is, it is not possible to secure efficiency and honesty in the conduct of the financial affairs of the State. It is not enough for the Legislature and the Government to specify the amounts of and the conditions under which the public money is to be spent. It is also necessary to have an agency for ensuring that their intentions are duly carried out in practice. The necessity for the audit of public accounts arises in order to find out whether the financial regulations and the programme of public expenditure laid down by the supreme authority are adhered to. The deviation from general policy or the standing rules, which have been laid down for its execution, are offences that are bound to occur. But their gravity or frequency can be considerably reduced if the financial acts of the public officers are examined by an independent authority and the irregularity or otherwise adjudged. In financial affairs, more than any other sphere of public service, the executive officers are concerned more with keeping things unknown than leaving them undone. It is the function of the audit officers to bring to light facts which would otherwise remain undetected. The audit, if it is to be sufficient, should be conducted by officers independent of the executive officers whose accounts they examine. The subordination, direct or indirect, of the former to the latter

detracts from the value of audit, and makes a frank and fearless expression of opinion very unlikely. The audit officers are expected to sit in judgment on the financial acts of the executive officers, and if they are to perform their function without fear and favour, they must not in any way be under the latter. They are as a matter of fact the counterpart of judicial officers in the financial organization of the State, and anything that reduces their independence must militate against the quality of their work or the impartiality with which they perform it. It was once held —a view which bore the imprimatur of the Welby Commission—that it was against the public interest to make the audit authorities independent of the executive authorities, for it was undesirable to adopt a measure which might suggest to the people of India that the Government of India required to be checked in the auditing of its expenditure by an independent authority set up in India.[1] This was in keeping with the theory of entire administration. But this view has now been abandoned, and an attempt has been made, as a part of the recent constitutional changes, to make the audit officers independent of the Government of India. It is now recognized that the audit cannot be efficient unless it is independent. In England the House of Commons was, in spite of its eagerness to make its financial control real, for a long time satisfied with the restrictions that it imposed on the issue of money from the Exchequer. It, to quote from Lord Welby's memorandum, submitted to the Select Committee on National Expenditure in England, "remained under the illusion that it could control expenditure by putting checks on the issue of money from the Exchequer instead of ascertaining how the money has been spent." But since 1866—the year in which the foundation of the present system of audit was laid in England—the House of Commons has been exercising very effective control on the public expenditure by securing its early audit and then examining the results of audit through its own committee. The financial control of the Legislature

[1] *Vide* Welby Commission Report, Vol. IV, para. 89.

in India cannot acquire a reality, unless we have an audit agency which will scrutinize the receipts and expenditure on their behalf and safeguard the interest of the taxpayer against the inroad of the official infractions. The importance of an effective and well-organized system of audit in the scheme of national finance cannot be overrated. If the audit officers realize the true significance of their duties, they can enforce the principles of financial rectitude, regularity, and propriety in the practical working of our financial system. It is to them that the Legislatures must look for expert advice and guidance when the mechanism of finance shows signs of working with an undue amount of friction or its positive results fall short of expectation. This, of course, takes for granted that the audit officers will not merely take a mechanical view of their duties and bring to bear an attitude to their performance not inconsistent with the highest ideals of public service.

The audit officers have, in the present constitution of India, a triple responsibility. They have in the first instance to watch the working of the financial system on behalf of the Secretary of State, the supreme authority in Indian finances, and ensure that the departure from principles, which he has laid down or approved, are as few as possible.[1] They have further to see that the expenditure

[1] The present Auditor-General in his memorandum on Audit under the Reforms, while emphasizing the importance of audit under the Reforms, says: "The work of the audit officer will inevitably increase in importance as the Reforms Scheme comes into effect. In paragraph 260 of the Report (the Joint Report) the authors state that 'on the other hand, it should be made plain to them (the Goverment of India) that if certain functions are maladministered, it will be open to them, with the sanction of the Secretary of State, to retransfer subjects from transferred to the reserved list or to place restriction in the future on the Ministers' powers in respect of certain subjects." If ever such action has to be taken, its need will have to be proved by the records of the local Finance Department in their relation with the Ministers, and by serious financial irregularities perpetrated in connection with the transferred subjects brought to light in the Appropriation Report of the Auditor-General and the local Accountant-General. If this conception of the audit officers' duties is accepted as correct, they are to watch the working of the Reforms in their financial aspect and will, when the time for the revision of the constitution comes, be required to pronounce the judgment on the financial actions of the ministers, and advise for or against the grant of wider financial powers to the Legislature under the

which requires his previous sanction is not incurred unless the sanction has been obtained. They have, in the second place, to conduct their audit on behalf of the Government of India and the Provincial Governments, which grant funds for non-voted heads of expenditure and whose sanction, or those of the authorities to whom they delegate the power, is necessary for incurring expenditure. In the third place, they have to audit expenditure on behalf of the Indian Legislatures for those heads of expenditure which are subject to their vote and report to them all cases when the expenditure relating to such items has been incurred without adequate authority, or funds granted for one purpose have been diverted to another. The last function has been entrusted to them as a result of the Reforms and must, as the financial powers of the Indian Legislature are enlarged, grow in importance. The Auditor-General in England has got dual function. He audits on behalf of the Parliament and the Treasury. In India the work of audit and the system of classification with which it is closely connected are more complicated, and the fact that the Government has undertaken activities of a quasi-private character makes it more varied and different. The vast extent of the territory over which the financial operations of the Government are spread, and the existence of the different administrative authorities makes audit necessarily decentralized and requires special arrangements by which the whole financial arrangements can be brought under review, and the results of experience collated with one another. The grant of financial powers to the Legislatures has introduced a new element which will take time to work out its full effect, but which will ultimately become the most important factor in the whole system of audit in India.

To understand the real purpose of the Government audit

revised constitution. It makes them to the extent to which this function is real, the principal witnesses on whose evidence the British Parliament will base its decision with regard to the grant of the wider financial powers to the Legislatures, when it, "with due regard to the due discharge of its responsibilities" for the welfare and the advancement of the Indian people, can persuade itself to grant us another instalment of self-government.

it is helpful to compare it with the commercial audit. It is a matter of common knowledge that every well-managed corporation gets its financial position examined by the trained auditors, from time to time, who are expected to be absolutely unconnected with the concern. In some respects the Government and commercial finance are similar. In both it has to be ascertained whether the expenditure has been incurred with the sanction of the competent authority, whether the system of accounts is suited for the purpose for which it is intended, and to what extent the accounts represent the actual facts to which they refer. But the main purpose of the commercial audit is to examine the financial standing of the business from the point of view of its earning capacity. Is it paying ? That is the principal object of their enquiry. Everything else is subsidiary to this all-important function. A business concern exists for earning profits, and it is the duty of the auditors to scrutinize its accounts with a view to pronounce judgment from that point of view. Have all the liabilities been brought to account ? Has the income been correctly calculated ? Has the permanent equipment been kept in a state of good repair ? Has the provision been made for its replacement after the expiry of the normal period of its life ? These and such other questions are directed towards assessing the profit-earning capacity of the concern and making sure that the accounts have not been manipulated to give a misleading idea of its real financial position. The Government audit, on the other hand, has a different purpose. Leaving out of account those activities which are of a semi-commercial character, and which in India are important, the Government audit is undertaken with a view to find out whether revenue is raised according to the principles and methods approved by the supreme authority, whether the expenditure is incurred for purposes specified by it, and whether the amounts sanctioned for each purpose are not ordinarily exceeded without the sanction of the competent authority. The Government is not a business corporation. It exists to promote the public welfare—the

object for which the citizens pay taxes. The audit officers cannot question the financial policy and programme of the Government. But taking that for granted, they have to ascertain whether the machinery and the methods by which both are carried out are adequate for the purpose, and are not used for ends other than those for which they are designed. The Government has laid down certain financial rules, which the knowledge of the principles of sound finance or lessons taught by the past experience has suggested. The audit officers have to say how far the rules are suitable or effective. They are the custodians of public interests. They cannot remedy the defects of policy or have any hand in shaping it; but they can do what is not less important—they can enquire into its execution and say how far the public interests have been safeguarded in every possible manner. The vitality of the public audit depends, to a certain extent, upon the existence of the effective control of the taxpayers on the methods of raising and spending money. The extent to which this control is absent in India makes the control less valuable from the point of view of the public. But apart from this consideration, the principles on which a sound system of audit is to be conducted are the same all the world over and do not vary with the temperature of a country or the character of its political institutions. The fact that the Legislatures do not possess a determining voice over the whole field of financial administration makes the necessity of having a really vigilant audit all the more imperative. Another point of difference between the Government and the commercial audit is, that while the latter is periodical, the former is continuous. It takes place soon after the expenditure is incurred, and malversation of public money or irregularity in spending it are detected a few weeks after their occurrence, and steps taken either to recover the amounts from the delinquents, if that is necessary or possible, or otherwise bring the matter to the notice of the higher authorities, who are expected to take the necessary action in the matter and report its nature to the audit officers. It then rests

with the latter to say whether the action taken by the executive authorities is adequate, and commensurate with the gravity or the character of the offence. It is not the remunerativeness of the financial operations which is of consequence in the audit of public accounts; it is their regularity and soundness in respect of economy and efficiency that matters. The independence of the audit agencies is important both in Government and commercial audit, the methods employed are also similar in some respects, but the essential purpose of audit is different in each case. The difference is fundamental and springs from the nature and the organization of the Government.

The audit of the Government receipts in India is of a simple character. It is sufficient to see that all sums which are payable to the Government have been duly paid to the proper officers, and brought to account by them. The difficult part of the audit of receipts is the necessity of checking whether all proper claims of the Government have been enforced. The chief source of the public revenue are the taxes. It is difficult to ascertain whether all persons on whom the taxes are to be levied have had their liability properly assessed, and paid the amount due to the collecting officers. The audit officers do not apply any check on the assessment and collection of almost all the taxes, that duty being entirely left to the revenue-collecting authorities. This is an important defect of the system of audit in India. In England the Auditor-General audits the receipt of revenue from various taxes on behalf of the House of Commons and submits the results of the audit to the House. The control of the Indian Legislatures over taxation is more complete than over the expenditure. There are no non-votable taxes, though land revenue has still to be put on a statutory basis. It should be the duty of the audit officers to exercise some kind of check over the methods of assessment and collection of taxes. It may perhaps be sufficient to audit certain classes of receipts or the receipts pertaining to particular periods, examine the general procedure and the regulations framed by the revenue departments to

enforce a proper standard of efficiency in the work of the collection of the taxes. It is well known that the administrative side of our tax system admits of considerable improvement. The institution of the audit of receipts will not do everything, but it will certainly supplement the other measures which may be taken for effecting the necessary changes for the better. The receipts of the Government from sources other than taxes are subject to audit to a certain extent. Of these the most important are the receipts of the commercial departments, which are examined in the audit offices of the departments concerned to see that the persons to whom the services have been rendered have been properly charged, and the amounts paid by them credited in the Government accounts. The receipts arising out of the disposal of the Government stores, sale of public property or the recovery of public advances to the private individuals, or the public bodies are fully checked and carefully watched to see that the amounts due to the Government on account of these transactions are paid into the treasury. There is another class of receipts which arise not on account of the claims of the Government to receive money, but which nevertheless requires to be checked. They are money order receipts, Postal Savings Bank deposits, and other receipts, which are credited to the Remittance or Debt divisions of the accounts. In this respect the audit can exercise no function as to their receipt. But their repayment has to be checked and also the fact that they are in respect of the amounts originally paid verified. The other function of audit with regard to receipts is to ensure that all amounts received on behalf of the Government are brought to credit in the accounts. The amounts, as already stated, are either paid direct into the treasury, or to the officers of the revenue departments who are to remit them to the treasury. As it is not possible to collect receipts given to the persons who pay the amounts, the method by which the check is exercised is to compare the receipts shown in the accounts of the collecting departments with the corresponding

credits in the treasury accounts. For this purpose extracts from the monthly returns of the treasuries are sent to the revenue departments (like Income-tax, Excise, etc.) which they are to compare with the amounts credited in their accounts, and receive from the Commercial, Public Works, and other departments information regarding their payments into the treasuries, which the Accountants-General compare with the treasury credits. The differences which the comparison may bring to notice, are then taken into consideration, and the two sets of accounts reconciled. In this way the errors are corrected and possibly a few frauds detected. This check is effective as far as it goes, but on the whole it has to be admitted that the audit authorities play a very limited part in scrutinizing the Government receipts, and protecting it against dishonest or accidental omissions to realize its enormous cash dues. This is due to the general difficulty which the audit officers experience in getting into immediate contact with the primary facts of public finances, but can be partly overcome if the fuller examination of the Government receipts from taxes is also made the duty of audit officers. A great deal must necessarily depend upon the revenue officers, but a knowledge that their methods and practices would, as a matter of course, be enquired into, will make them more assiduous and upright in the discharge of their duties. Audit cannot go further than make the neglect of duty, culpable or careless, a little less safe or easy. It, like everything else, has got its own limitations.

The audit of expenditure is a dual function. In the first place it has to be ascertained whether money has been provided in the budget for a particular object of expenditure by the Legislature or the Government, or, in other words, the expenditure has to be audited against appropriations. In the second place, it has to be verified whether sanction for spending money for the particular purpose has been accorded by a competent authority, or the expenditure has to be audited against sanctions. This, it will be remembered, is in accordance with the fact that for incurring

expenditure two conditions have to be fulfilled. The appropriation has to be made by the Legislature or the Government, and the sanction accorded by a competent authority. The audit officers have to see that every outlay of public money satisfies these two essential conditions, and if it does not, he has to place the amount in question under objection, and take necessary steps to regularize it, or report the matter to the higher authorities for disciplinary action. In the audit against appropriations, the grants have to be examined, and it has to be seen whether for votable expenditure they have been covered by the vote of the Legislature and for non-votable expenditure by the authority of the Government. The appropriation and reappropriations within a grant have to be similarly looked into with a view to see that they have been made by a competent authority, and do not increase the amount of the grant without adequate sanction. The expenditure against grants and the units of appropriations within them is watched to see that it does not exceed the sanctioned amounts and when the excesses are likely, the officers concerned have the necessary warning issued to them in time to enable them to obtain the required sanction. As an aid to the audit against appropriations, it has to be further watched that the expenditure chargeable to one grant or unit of appropriation is not debited to another, and whenever a unit of appropriation is distributed among a number of spending officers, each one does not exceed his allotment. In audit against sanctions the first thing that has to be ascertained is that all expenditure which requires the sanction of the Secretary of State has received his sanction. Each executive authority has got its own financial powers within which it can sanction expenditure at its own discretion. The Central and the Provincial Governments can sanction expenditure within the limits laid down in the Audit Resolutions and can delegate their powers with the previous consultation of the Finance Department to the authorities subordinate to them. The audit officers in examining expenditure have to see that the various

administrative authorities do not exceed their financial powers. In accepting the sanctions accorded by the different administrative authorities, the audit officers have to satisfy themselves that the conditions which limit their exercise have been duly fulfilled, or in other words these sanctions themselves have to be audited. Besides these two important functions the audit officers have to bear in mind a number of other considerations in going through the public accounts. They have to see that they are supported by proper documents or vouchers, payment has been made to persons entitled to receive it, has been duly acknowledged, the classification of expenditure is correct, and rules laid down by the Government for the conduct of the financial business have been fully observed. The officers have further to satisfy themselves that what are called the canons of financial propriety have not been in any way infringed. These canons are not statutory rules or the orders of the Secretary of State. They are merely the general tenets for the management of public finance, and the responsibility for seeing that in the whole range of public expenditure, whether Central or Provincial, voted or non-voted, reserved or transferred, the spending officers act upon them, has been laid on the audit officers. The advent of the popular Government in the country makes the need of independent and efficient audit greater than before. Democracies fight shy of experts, but in matters of finance it is not possible to get on without them. The outgoings of the State are so varied and numerous that without a proper system of audit it is not possible to prevent improper expenditure of money. Nothing should be done which may, directly or indirectly, weaken their hands. The future changes in the political system of the country should raise their position to enable them to act with courage, discrimination and knowledge in the performance of their important duties.

There is another class of transactions whose audit is a matter of some importance. The Government spends very large sums in the purchase of stores. The Railway, Posts

and Telegraphs, Public Works, and Military Departments need a variety of materials for their requirements. It is not enough that public money be followed till it has been spent in the purchase of stores, and then leave it to the administrative officers to use them as they like. The use and the issue of stores have also to be carefully watched. It is easier to exercise a check over the issue of cash than that of clothing, victuals, coal, and numerous other things in the purchase of which the Government spends crores every year. The audit officers have to see that every article which is purchased on Government account is credited in the store returns. They have to link the credits in the store returns with the documents on which the payments have been made, and compare the rates paid with those shown in the contract for the supply of stores. The issue of stores from the stocks have to be watched to see that it is made only to persons who are authorized to draw them and not in excess of sanctioned scale. Every issue has to be supported with the receipt of the person to whom it is made. The balance in the hands of the storekeepers has also to be checked. In India the check is left to the administrative officers, who have, from time to time, to verify whether the quantities shown in the accounts agree with the quantities actually in stock, and the audit officers accept the reports of the administrative officers as correct. It is difficult to say how far the absence of outside check by the audit officers leads to a loss of public money. But the reasons which make the independent audit of the receipts and expenditure necessary are equally valid for the examination of the store accounts and stocks. As the purchase of stores entails the expenditure of large amounts of money, it is desirable that unduly large quantities should not be purchased in advance of the actual requirements. It is necessary to keep some stock in hand, but if it is larger than what is warranted by the necessity of the circumstances, it, besides involving loss of public money on account of the possibility of stores being damaged or rendered unfit for some reason or the other, means a lock-up of the public

funds and a loss of interest thereon. The Inchcape Committee estimated that the total value of stocks of stores held by the various departments of the Central Government amounted to the huge sum of about 60 crores, which on a moderate estimate means a charge of about 3 crores every year on account of interest on the amount in question. The progressive reduction of these large holdings, which the Inchcape Committee has recommended, can be brought about if the Government of India and the departments concerned set their face against the accumulations of the valuable materials, but the audit officers can, within certain limits, render some assistance in the execution of a less costly policy in this respect. Purchase of stores has, of late, attracted a considerable amount of public attention on account of the need of making it a means of giving stimulus to the industrial development of the country. The Government of India has now established the Indian Stores Department on a permanent basis, and proposes to foster the growth of the indigenous industries through its operations. But the policy of the purchase of stores needs revision from the standpoint of economy and the prevention of waste. The popular belief is that in the purchase and the maintenance of stores, public interest is generally sacrificed, and there are great many practices prevalent in the stores branches of the various departments which have to be put down with a very strong hand. An effective audit of the store accounts and stocks will be helpful in eliminating waste, carelessness, and dishonesty in the buying and handling of Government stores.

When the audit officer discovers an irregularity in the accounts, it is his duty to communicate it to the officer concerned. If an excessive or an irregular payment has been made, he has to order the recovery of the amount. The recovery has to be effected unless the payee can give satisfactory explanation as to why it should not be made or wants to appeal against the audit decision to the higher authorities. But in a number of cases it is not necessary to effect recovery. The necessity of placing an item under

objection arises for want of vouchers, for want of appropriation, or the sanction, for excess over the appropriation or insufficient sanction, or for the contravention of any canon of financial propriety. In such cases the explanation is called for from the administrative officers. The objections have to be promptly communicated to them, and the latter are required to give them their immediate attention. If a wanting voucher is submitted, additional appropriation or sanction obtained from the competent authority or an explanation furnished which the audit officer considers satisfactory, the objection is removed. But if a satisfactory explanation is not forthcoming, the matter is reported to the head of the department, who is to take necessary action against the offending officers. If the audit officer is satisfied with the action taken, the objection is removed. But if he considers that the action taken by the head of the department is inadequate, he reports the matter to the Finance Department. It is not sufficient for the audit officers to raise the objections; they have to pursue them till they are cleared by the recovery of the amount due, further explanations, grant of appropriations or sanctions, disciplinary action or report to the Legislature or the Government. A record of the objections has to be maintained and reviewed from time to time. The results have finally to be included in the Audit and the Appropriation Reports, the nature and the scope of which is explained later. In doubtful matters reference has to be made to the Auditor-General, who is the final authority in audit matters.

There is, besides the audit of accounts, provision for the inspection of the audit offices by the assistants of the Auditor-General, and the inspection of treasuries, public works accounts, accounts of military units and other local account centres, by the officers of the Audit Department. The Auditor-General is responsible for the efficiency of the audit of India. He does not conduct the audit himself, but he institutes from time to time what is called test audit—that is, he deputes the Deputy Auditor-General to go to

the provinces and the military audit circles known as the commands and examine in details the accounts of a portion of expenditure, and submit a report to him on the results of the examination. From these reports the Auditor-General can form a judgment on the efficiency of audit. The visits of the Deputy Auditor-General are the means by which the Auditor-General satisfies himself that the detailed audit conducted by the provincial and the departmental audit officers is efficient, that the regulations and the orders of the Government are duly enforced, and that the procedure in those offices is suitable for the satisfactory discharge of the audit and account duties. The Deputy Auditor-General occasionally inspect the Railway and Military Audit Offices, but they are primarily concerned with the inspection of the Civil and Posts and Telegraphs Audit Offices. The detailed inspection of the Railway and the Military Audit offices is carried on by departmental inspecting officers. The inspections of the treasuries, public works, military, and other local accounts are arranged by the audit officers, and the reports are sent to the heads of the departments concerned to enable them to remove the irregularities which may thus be discovered. The inspecting officers are expected to assist the officers whose accounts they examine, to remedy the defects, and suggest the means by which the repetition of the mistakes can be prevented. Their function is to educate as well as investigate. In a vast country like India it is not possible for the Audit Officers to come in close contact with the activities of the spending officers. The inspection, if it is thorough and efficient, is the only way by which a uniform standard of efficiency can be achieved, and co-ordination of activities secured. It is possible to carry the passion for uniformity a little too far, but in the case of the departments whose activities are spread all over the country, local autonomy can only lead to local anarchy. The Inspecting Officers with their experience, training, and broad outlook can be of great use in impressing on the local officers the need of remembering that they are parts of a

greater whole, and the efficient working of the whole depends upon the parts working well.

The Government of India have, in their conception of the part which the audit is to play under the new constitution, laid considerable stress on what they call higher audit. The complaint against the Audit Officers in the past has been that they have been weighed by the multiplicity of rules which they were called upon to interpret and apply, that the insistence on technical fidelity has been created too far, and trivial matters have given rise to correspondence and consequently work for all concerned, which the exercise of the saving grace of common sense could easily have avoided. The Government of India, in their Reforms despatch, which has been so frequently quoted, after pointing how audit in the past has been obsessed by codes and formalisms, and how under the new conditions tangled mass of rules and regulations would have to be cleared, and reliance placed more on discretion and judgment rather than the mechanical industry, go on to say: "In place of formal examination of authorities and rules the work (of audit) should be conducted with greater regard to the principles of legitimate public finance. The audit will not only see whether there is quoted authority for expenditure, but the necessity of it. It will ask whether the individual items are in furtherance of the schemes for which the budget provided, and whether the same result could have otherwise been obtained with greater economy; whether the rates and scales of pay were justified under the circumstances; in fact they will ask every question that might be expected from an intelligent taxpayer bent on getting the best value for his money." In pursuance of the intentions expressed in this quotation a separate branch has been constituted in each audit office consisting of picked men, who are charged with the duty of introducing a spirit of enquiry into the work of audit. The business of this section is conducted under the personal guidance of the Accountant-General. It is too early to say as to what measure of success has been achieved in this matter. A

great deal of spade work has to be done in order to effect a real breach with the traditions of the past. A tangled mass of regulations has to be cleared, codes recast, and a set of fundamental rules and principles evolved for vitalizing the system. All this will take time. The public and the Legislature can accelerate the growth of the new traditions by appreciating the importance of the audit and insisting on its conduct in the right spirit. The work of audit requires the services of public-spirited and capable officers, who can be depended upon for safeguarding the interest of the taxpayers in an adequate manner and securing a conformity to what have been described as the legitimate principles of public finance.

The audit and administrative functions cannot be sharply demarcated. It is difficult to draw a line where the sphere of one ends and the other begins. The Audit Officers are asked to bear the distinction between the audit and executive functions in mind and not to trespass in the domain of the Executive Officers. In theory it is possible to say that the Executive Officer has to do the work and the Audit Officer to report on it. The latter has neither the opportunity nor the capacity to deal with the basic facts which the former has got to take cognizance of. There are certain matters in which the discretion of the Executive Officers cannot be questioned. But they are apt even to resent those enquiries of the Audit Officers which are necessary for the discharge of the duties that have been laid upon them. It is the function of the Finance Department to help the various Executive Officers to appreciate the nature of the work which the Audit Officers have to do, and enable the latter to pursue their investigation without any friction. A close and cordial co-operation between the Audit and the Finance Departments is necessary for the efficient working of the financial system. The Finance Department, being in charge of the financial administration of the country, has itself to run the gauntlet of the audit scrutiny. But it has also to render material assistance to the the Audit Department. The Audit Officers have to rely

upon the Finance Department for knowing the intentions of the budget scheme or of the financial rules that they have to apply. There are a number of other facts relevant to audit, the knowledge of which cannot be obtained by the Audit Officers without having recourse to the Finance Department. The Audit Officers assist the Finance Department in the preparation of the estimates and securing adherence to the scheme of appropriations. This is due to the combination of the audit and account functions, for the latest figures on which the Finance Department has to rely are available in the office of the Accountants-General. The compilation of accounts being done in the same offices, the Audit Officers are in a position to watch the growth of the expenditure and compare it with the sanctioned estimates. The plea for making a clear distinction between the audit and excutive functions and separating the audit and account duties, which is urged at the close of this chapter, will not, when given effect to, make the Audit and the Finance Departments rivals or even mutually-apathetic organizations. It will still be necessary for both to practise mutual aid in order to promote economy, regularity, and efficiency in the financial work of the State—the objects in which both are keenly interested. The separation of functions is a convenient way of transacting financial business. It does not obviate the necessity of working together with perfect harmony, and affords plenty of scope for joint and reciprocally advantageous work.

The Audit Offices cost the taxpayers a substantial amount of money. The question has often been asked whether there is any adequate return for this outlay. Is there any saving effected as a result of the activities of the Audit Departments ? This question shows a misconception about the work of the Audit Officers. It is well known that the very existence of preventive establishments is a great advantage. It has a deterrent effect on the wrong-doer. If it is known that the chances of an offence being detected are greater than of its remaining unnoticed, it is

likely that it will not be committed. The fact that the accounts of the public servants are regularly examined and irregularities brought to the notice of the higher authorities, is bound to have a wholesome effect on their conduct and give a keener edge to their sense of duty. But besides this consideration there are two others which have got to be borne in mind in this connection. The Audit Officers have no voice in moulding the policy of the Government and cannot question it. If the Government decides to have a certain number of British soldiers in India, and fix a particular scale of pay, clothing, and rations, the Audit Officer cannot point out the injustice of not engaging the Indian soldiers instead, who cost much less. He can have nothing to say against the policy of retaining a certain number of Europeans in the higher services, and paying them liberally in order to make their work attractive for them. He must accept the decision and see that the pay and allowances drawn by the officers are not in excess of the sanctioned scale. Again, if the Legislature votes a large sum of money for a University, which in the opinion of some is a costly luxury, or is determined to have a magnificent council chamber worthy of the dignity of the law-makers of the country, irrespective of the expense involved, he must once more adopt a quiescent attitude in the matter and refrain from raising any objection. The Audit Officer has to perform important duties in the financial organization, but sitting in judgment on the decisions of the fund-granting authority is not one of them. He audits the expenditure on behalf of that authority and if the Government or the Legislatures themselves do not remember the limits of the taxable capacity of the people while granting money, he may regret the fact, but he cannot criticize, much less undo it. It has been said of the Judicial Officers that they administer law and not justice. The Audit Officers, it has been said already, occupy a position analogous to that of the Judicial Officers, in the financial organization of the State. They have to apply the financial rules with judicial impartiality, but not change their

purport. They have some scope for introducing the personal element in the interpretation of the rules in cases which are not fully covered by the rules. There are case-made rules as there are case-made laws. But they cannot go further. They must as a rule take the decision of the Government or the Legislature as final and supervize its execution to see that every officer acts within the limits of his own financial powers, without contravening the letter or the spirit of the orders of the supreme political authority. This limitation of the Audit Officer will continue even when India is completely self-governing, and the Legislature the final authority in the national finances. Unfortunately there is another limitation as well, which reduces the power of the Audit Officers in effecting economies in the national expenditure. They, on account of the difficulties inherent in the nature of things, cannot have direct knowledge of the elemental facts on which the accounts are based. The first canon of the financial propriety, which every public officer has to act in accordance with, is that he should exercise the same vigilance in respect of expenditure incurred from the Government revenues as a person of ordinary prudence would exercise in respect of expenditure of his own money and the Audit Officer has to see that he does so in actual practice. His power to enforce the consideration of economy is, however, circumscribed by practical difficulties. When abnormally high rates are being paid for getting some work done, or there is some other case of patent extravagance, he is to draw the attention of the Finance Department to the fact in order that the remedial measures may be taken. But the cases that he can take notice of must be such as to invite enquiry on the basis of accounts or documents submitted to him. He generally cannot examine the facts which the accounts record. His inspections may perhaps enable him to find out some crude malpractices which he could not have discovered from the accounts. But if the initial accounts are well manipulated, the cases of dishonesty or neglect of duty can defy the most searching examination by the Audit

Officers. If the Executive Officers certify that a certain number of labourers were engaged, when the actual number was much less or the quality of the goods delivered or the soundness of the building constructed attained the required standard, the Audit Officer has no other alternative but to accept the testimony as conclusive. If the statements do not agree with facts, he is helpless in the matter. The best way of preventing waste or the misuse of public money is to provide adequate supervision from within the department itself, and if that cannot put an end to the evils, nothing else will. The Audit Officer has to depend upon the accounts, which he can have access to; and it must be an unusually incautious officer whose accounts tell damaging tales about himself. In spite of this handicap, the Audit Officers do discover cases which call for action of a deterrent character. But they are few and often not very grave. Audit can supplement the administrative vigilance and the sense of responsibility of the public servants. It cannot take their place. If corruption and carelessness are rife in a department, it is not possible to uproot them by instituting a more thorough audit of accounts. These are the evils which require much more drastic measures, and even they will be of no avail, if the mentor within and the public opinion are prone to take an indulgent view of their existence.

The collective results of audit are embodied in the Audit and Appropriation Reports. These are documents of very great importance. They have, since the introduction of the Reforms, acquired a new importance, for in so far as the votable expenditure is concerned, they are the reports on the financial administration of the Government to the Legislature and are intended to enable the latter to pass judgment on the efficiency of work of the former. These reports were formerly in the nature of the reviews of the financial events of the year—a rehash of the questions disposed of twelve months before, as an ex-Finance Member slightingly styled them. In England the Auditor-

General submits a report to the Parliament on the financial irregularities of the Government as a whole. The Parliament which votes supplies has a report placed before it by an officer independent of the Executive to enable it to see whether the expenditure has been incurred in accordance with the grants, and acquaint himself with the manner in which the financial administration of the country has been carried on. In India the supplies are partly voted by the Legislature and partly granted by the Executive. In so far as the Legislature grants money and the Executive spends it, there is some analogy between the Audit and Appropriation Reports in India and the reports of the Auditor-General in England. But the analogy breaks down in case of those parts of the reports which deal with expenditure not submitted to the vote of the Legislature. The Executive grants and spends money and has a report submitted to itself on the expenditure of the year. That comes to this, that to use the words of Lord Welby, the Government knows at the end of the year whether they have been of the same mind as at the beginning of the year, which is no advantage from the point of view of bringing the action of the highest executive under the review of an outside authority. This is an important aspect of the whole matter, and has to be borne in mind in this connection. The bearing of these remarks will become a little clearer if the nature and the manner of disposal of these reports is explained at some length. The Audit Reports, which are generally ready by 10th September of the year following that to which they relate. They deal with the important financial irregularities, other than those connected with appropriations, discovered during the year in the course of audit. All cases of serious financial irregularity, statistics of the expenditure placed under objections excluding the objections relating to appropriations, an account of the activities of the Audit Department, and a few other relevant matters are included in the Audit Reports. The figures are analysed and tabulated to give an idea of the kinds of the irregularities which are most

frequently committed. The Appropriation Reports contain a review of the financial situation as a whole, an account of the changes in the classification of accounts, appropriation accounts, and explanation of excesses and the results of appropriation audit against the units of appropriations. The reports differentiate between the expenditure pertaining to voted and non-voted heads and in the case of the provinces also between the reserved and the transferred. The Appropriation Reports are ready in February of the year following that to which they relate. The reports dealing with the civil expenditure of the Central Government are prepared by the Accountant-General, Central Revenues, and those dealing with the Military, Railways, Posts and Telegraphs, expenditure by the Accountants-General of the departments concerned. The Audit and the Appropriation Reports of the provincial expenditure are prepared by the provincial Accountant-General. All these reports are submitted to the Auditor-General who transmits them with his own remarks to the Finance Department of the Government concerned, and also to the Secretary of State through the Governor-General in Council with such remarks as he may consider necessary to make. The Finance Departments submit these reports for the consideration of the Public Accounts Committees, and when the latter have formulated their own conclusions on them, the Finance Departments forward to the Audit Officers and the Auditor-General reports of the Public Accounts Committees, the orders of the Legislatures thereon, and a statement giving an account of the action taken by the Government to give effect to the views of the Legislatures. The orders passed by the Government on the non-voted heads of expenditure are also communicated to the Audit Officers.

The Public Accounts Committees referred to above are the committees of the Legislatures for the consideration of the Audit and Appropriation Reports. They are the statutory bodies which contain a majority of elected members, only about one-third of the members being

nominated by the Government.[1] Each province has got its own Public Accounts Committee, and there is one for the Central Government. The Finance Member of the Government concerned is the chairman of the committee. It deals with the Audit and Appropriation Reports and specially examines cases of reappropriation from one grant to another and reappropriation within the grant, and any other matter that the Finance Department may submit for its consideration. The Accountant-General, and in some

[1] The constitutions of Committees of Public Accounts, the central and the provincial, are laid down in the Legislative Rules framed under the Act.

For the Committee of Public Accounts of the Assembly the following rules have been laid down:

"51. *Constitution of Committee on Public Accounts.*—(1) As soon as may be after the commencement of each financial year a Committee on Public Accounts shall be constituted for the purpose of dealing with the audit and appropriation accounts of the Governor-General in Council and such other matters as the Finance Department may refer to the Committee.

(2) The Committee on Public Accounts shall consist of not more than twelve members including the Chairman, of whom not less than two-thirds shall be elected by the non-official members of the Assembly according to the principle of proportionate representation by means of the single transferable vote. The remaining members shall be nominated by the Governor-General.

(3) The Finance Member shall be Chairman of the Committee, and, in the case of an equality of votes on any matter, shall have a second or casting vote.

52. *Control of Committee on Public Accounts.*—(1) In scrutinizing the audit and appropriation accounts of the Governor-General in Council, it shall be the duty of the Committee to satisfy itself that the money voted by the Assembly has been spent within the scope of the demand granted by the Assembly.

(2) It shall be the duty of the Committee to bring to the notice of the Assembly:

(i) Every reappropriation from one grant to another grant;
(ii) every reappropriation within a grant which is not made in accordance with such rule as may be prescribed by the Finance Department; and
(iii) all expenditure which the Finance Department has requested should be brought to the notice of the Assembly."

For the Committee of the Public Accounts of the Provincial Legislature the following rules have been laid down:

"33. *Constitution of Committee on Public Accounts.*—(1) As soon as may be after the commencement of each financial year a Committee on Public Accounts shall be constituted for the purpose of dealing with the audit and appropriation accounts of the Province and such other matters as the Finance Department may refer to the Committee.

(2) The Committee on Public Accounts shall consist of such number of members as the Governor may direct, of whom not less than two-

cases the Auditor-General, attends the meetings of the committee and helps it in the examination of the reports and irregularities. The heads of the departments and other officers of the department can also be required to give oral explanation, which, however, cannot be easily obtained on account of the distance at which the officers do their work from the head-quarters of the Government. The Committee is concerned merely with voted expenditure, non-voted items being excluded from its purview. The Committee submits its report to the Legislature which passes orders on matters brought to its notice. The Government issues a minute indicating the action taken by it in pursuance of the orders of the Legislature. These committees have been created to check and control the financial activities of the Executive in those spheres of the administrative work over which the Legislatures exercise some authority. They have been constituted after the model of the Public Accounts Committee of the House of Commons, which has since 1861 played such a prominent part in the examination of public accounts and become an important factor in the financial machinery of England. The Committee in England has a very wide range of duties. It is not merely concerned with formality of expenditure,

thirds shall be elected by the non-official members of the Council according to the principle of proportionate representation by means of the single transferable vote. The remaining members shall be nominated by the Governor.

(3) The Finance Member shall be Chairman of the Committee, and, in the case of an equality of votes on any matter, shall have a second or casting vote.

34. *Control of Committee on Public Accounts.*—(1) In scrutinizing the audit and appropriation accounts of the Province, it shall be the duty of the Committee to satisfy itself that the money voted by the Council has been spent within the scope of the demand granted by the Council.

(2) It shall be the duty of the Committee to bring to the notice of the Council:

(i) Every reappropriation from one grant to another grant;
(ii) Every reappropriation within a grant which is not made in accordance with the rules regulating the functions of the Finance Department, or which has the effect of increasing the expenditure on an item the provision for which has been specially reduced by a vote of the Council: and
(iii) all expenditure which the Finance Department has requested should be brought to the notice of the Council."

but also its wisdom, faithfulness, and economy. It exercises these functions in respect of receipts, expenditure, and store transactions. It is assisted in its work by the Auditor-General and a high officer of the Treasury. It examines accounts, calls for explanations, written and oral, and recommends measures for removing specific defects and for the general improvement of the financial system. The chairman of the Committee is by usage always a member of the "opposition" in order that the Committee may not overlook the shortcomings of the Government as a matter of party expediency. The scope of its powers is co-extensive with the whole field of the financial administration. "It considers the form in which the estimates should be submitted, it passes upon the question of the number of votes under which accounting should be had; it examines into the conduct of the Treasury, it satisfies itself whether economy and efficiency have been displayed by several services in the expenditure of funds; finally it pays special attention to the technical accounting procedure employed by the Government."[1] Its reports make a very valuable reading, and are, together with the Treasury minutes passed on them, the financial regulations for the guidance of the public officers.[2] The Committee has been able to attain its present position on account of the hard, earnest, and skilled labour of some of its members who have rendered invaluable and unostentatious services in keeping up the highest standard of financial rectitude in the transaction of the financial business. It is not an easy matter, to use the words of E. Hilton Young, "to press an enquiry home against a phalanx of experts." The Public Committees in India have, when compared with their

[1] *Vide* Willoughby's "Financial Administration of Great Britain," page 231.

[2] "This is evidenced by the fact that in 1911 the Comptroller and Auditor-General caused to be prepared and published an epitome of all the reports of this Committee since its establishment, with the Treasury minutes relating thereto, which was fully indexed in order that all accounting officers might readily consult the orders that have been issued and were in force governing accounting methods."—*Vide* Willoughby's "Financial Administration of Great Britain," page 231.

prototype, very limited powers. Apart from the exclusion of the non-voted expenditure from their scrutiny, which is due to the peculiar character of our political constitution, and inexperience and want of training on the part of the members themselves, which no constitution can remedy, the main function of the Committees is to enquire into the financial irregularities, specially those relating to the appropriation accounts. The questions pertaining to the form of estimates and the number of votes are under the control of the Finance Departments and the form of accounts is determined by the Auditor-General. The receipt and the store transactions do not find a place in the reports of the Audit Officers and they cannot therefore take cognizance of the way that these transactions are being managed by the Executive Officers. It is true that the members of the Committee can, if they take to their work seriously, build up conventions which will enable them to widen the sphere of their investigations by showing that they know their business and can rub it in a little. The Public Accounts Committee in England has acquired its present position by rising higher and higher on the stepping-stones of the previous precedents. But the present limitations of the Public Accounts Committee cannot be attributed to the faith of the framers of our constitution in the subtle and persuasive influence of the unpremeditated conventions. The limitations have been deliberately imposed in order to restrict the field of enquiries of the Committee. But the most anomalous feature of their constitution is the position which has been assigned to the Finance Members of the various Governments in their composition. Every Finance Member, as already remarked, is an ex officio chairman of the Committee, and the reports are submitted not direct to the Legislatures, but to the Finance Department for submission to the Committee. What would the critics of the financial policy of Great Britain say if the Chancellor of Exchequer, or rather the Finance Secretary—for the position of the Finance Member corresponds more to the latter than to the former—were appointed the chairman of

the Public Accounts Committee? They would consider the position ridiculous. The Public Accounts Committee is, there, presided over by a member of the "opposition" and is on that account above suspicion. In India the Finance Member is the chairman, and the Finance Secretary the nominated member of the Public Accounts Committee. These two officers should as much, if not more than anyone else, be put on their defence, and called upon to render an account of their stewardship. It is they who are responsible for the efficiency of the financial administration of the Government, and it is they who as members of Public Accounts Committee examine the state of the Government finances and decide as to how far all is well with them. The incongruity of the position has not escaped the observation of the present Finance Member, who, in his speech in the Legislative Assembly on the 23rd July, 1923, said: "The position of the Finance Member as an ex officio chairman of the Public Accounts Committee is not going to be a very easy one. He will be passing as a member of the Council of the Governor-General criticism on the Governor-General in Council, which will be rather difficult, and I am not sure that as a permanent arrangement it will really work." This anomaly cannot be justified by the transitional character of our constitution. It strikes at the very root of the idea with which the Public Accounts Committee has been constituted. The members of the Committee are new to their work. They do not understand the intricacies of finance and have in most cases neither taken pains nor shown any aptitude for mastering them. They need all the assistance which the members of the Finance and the Audit Departments can give, and it is therefore necessary that they should have free access to the deliberations of the Public Accounts Committee and give it the benefit of their expert advice and guidance, but it is wrong in principle that they should sit on the Committee and take part in its proceedings. It is not necessary to emphasize the importance of the members of the Public Accounts Committee being quite at home in

dealing with the Government accounts. The check which the Public Accounts Committee in Great Britain exercises upon the extravagant, or the unauthorized expenditure, or unwise methods of financial management is much more effective than the check of the House of Commons. The need of making the financial control of the Legislature in India real is much greater for obvious reasons. The observations which have been made in Chapter IV regarding the members of the Legislature acting with the sense of responsibility of the pioneers apply with special force to those who are elected to the Public Accounts Committees. If they are unequal to the task which they have to perform, the officials can look forward to having a comparatively free hand in managing the finances of India. The members of the Public Accounts Committee will have to make a firm stand for order, regularity, and economy in methods of public finance, and to do that successfully they will need "weapons from the armoury of specialized knowledge" as much as courage and appreciation of the value of these advantages. It is only three years that the Public Accounts Committees have been at work, and on account of radical changes in the composition of the Legislatures and the overshadowing importance of the political issues, they have not been able to settle down to their work. It is on that account too early to say anything about the manner they have discharged their duties. It is their possibilities which are more important than their achievements.

As the Public Accounts Committees are not allowed to deal with the accounts of the non-voted expenditure, the reports relating to them are disposed of by the Government, the copies sent to the Secretary of State only receiving departmental consideration. Before 1920 the whole expenditure, both the central and the provincial, was, to use the word which had not come into use then, non-voted. The Welby Commission was of opinion that as it was essential to an effective system of audit that the audited accounts of public expenditure together with the auditor's report thereon should be examined and finally

passed by an authority whose judgment had weight with the public, it was necessary to constitute those safeguards in the Indian system. They suggested that the appropriation accounts and the report of Comptroller and Auditor-General, as he then was, should be referred by the Secretary of State in Council to a standing committee, two members of which should have no connection with the India Office. The argument in favour of securing an independent examination of Appropriation Accounts have, if anything, gained in weight since 1900. A substantial part of the public expenditure is still non-voted. The suggestion for the constitution of what for the convenience of expression may be called the non-voted accounts committee, is likely to hurt the susceptibilities of those for whom the end of our political tutelage is in sight. That would mean that it is being presumed that the distinction between the voted and the non-voted heads of expenditure is going to continue for some time. If, however, it is taken for granted that the distinction cannot unfortunately be abolished for some time to come, it is better that non-voted expenditure should, after being audited, be submitted to the scrutiny of a committee than that it should be merely passed by the Government. The condition that its judgment should carry weight with the public still holds good, provided the public is understood to mean the Indian public. No arrangement can be satisfactory which does not allow the accredited representative of the Indian people to have some share in the examination of those accounts. A standing committee of the India Office whose members are known to have leanings towards anything but economy, even with the admixture of one or two outside experts, is likely to be the least satisfactory way of realizing the object.

The Appropriation Reports are ready in February following the close of the financial year, but cannot be examined by the Public Accounts Committees during the spring session of the Legislatures on account of the preoccupation of the members and the officials with the budget. They are examined just before the commencement of the autumn

session, the members of the committees being called early enough for the purpose to enable them to go through the reports and submit their own reports to the Legislatures after the commencement of the session. The reports of the Public Accounts Committees, and their consideration by the Legislatures that follow, taken together, mean the final disposal of the finances of the year. It takes about full three years for a year's finance to run through their natural course. The preparation of estimates of the year 1921–22, for instance, must have commenced in the autumn of 1920. The Appropriation Reports of 1921–22 were dealt with and disposed of by the Legislatures in the autumn of 1923. The career of the finances of 1921–22 was then closed. The accounts and the reports are thereafter of interest only to the students of finance, and the members of the Department of Statistics, who then hold their post-mortem examination.

The audit of the Home Accounts is conducted by the Auditor of the Indian Accounts in the United Kingdom. He is independent both of the Government of India and the Secretary of State. He is not a member of the Indian Audit and Accounts service. He is appointed by His Majesty by a warrant countersigned by the Chancellor of the Exchequer, and holds office during good behaviour. That ensures him an independent and secure position. He only audits receipts and expenditure realized in England, the transactions in India being outside his ken. He has not got anything to do with the maintenance, classification, and compilation of accounts. The work is performed by the Accountant-General of the India Office. This fact is of interest in view of what has been said later about the combination of audit and account functions. The Auditor, unlike the Indian Audit Officers, cannot finally disallow expenditure. He is directed by the Section 27(5) of the Government of India Act to signify his approval or disapproval of the accounts of the Secretary of State. This provision is in accordance with the nature of duties performed by the English Comptroller and Auditor-General, who brings matters, regarding which he raises

objections to the attention of the Treasury for determination as to what action is to be taken. This is due to the fact that the responsibility for action rests with the Treasury, and the Auditor-General is to draw its attention to the irregularities and then report the matter to the Parliament. That makes the distinction between the audit and executive functions very clear. The responsibility, not only for the preparation of estimates but the whole financial administration, is centralized in the Treasury, and nothing is done to impair it in the slightest degree. This is the corner-stone of the whole system of financial administration in England. The position of the Auditor of Indian Accounts has, as far as possible, been assimilated to that of English Comptroller and Auditor-General. But the most important duty which has been entrusted to the Auditor is that he is to watch the expenditure from the Indian revenues in England and to see that money out of them is not spent for purposes other than those which are properly chargeable to the Indian accounts.[1] It is an important provision, and if given effect to in the right spirit would be an effective safeguard. The Auditor can, for instance, question whether the capitation rate of £25 13s. is a reasonable charge on the Indian revenues. Such objections have been raised in the past, but when the charges have been agreed to by the highest authorities in England and in India, it would require a courage, unfortunately rare, to take exception to a charge which is to be borne by the Indian taxpayer. The report of the Auditor is laid before the Parliament through the Secretary of State, who also issues a statement of the action taken by him and communicates it to the Auditor, which, however, is not submitted to the Parliament. The accounts and the report of the Auditor thereon are not examined by any committee, though, so far as the irregularities relate to the voted expenditure, they are included in the reports which

[1] For items properly chargeable to the Indian revenues see sub-section 2 of the Section 20 of the Government of India Act.—*Vide* Appendix I.

the Auditor-General in India transmits to the Finance Departments for submission to the Public Accounts Committees. It would show a lack of the sense of proportion if we were to make much of the formal independence of the Auditor of Indian Accounts. It has not been of much use in protecting the interests of India in England though, as already said, cases are not unknown when the Auditor has expressed his inability to certify the correctness of the charge thrown on the Indian revenues. The significance of the independent position accorded to him lies in the fact that the conception of the right function of audit made it necessary for the English authorities to include this rather unusual provision in the conditions of his appointment. It would have offended the sense of propriety of the framers of the Indian constitution, if he had been placed in a position of subordination to the Secretary of State whose accounts he was to audit. The actual gain derived by India from this departure from general practice in making the Indian appointments has been small, but the integrity of the conception as to what the duty of the auditor ought to be, has been kept intact. It may be added that the accounts of the High Commissioner are also audited by the same officer.

It is not necessary to devote much space to the explanation of the organization of audit and accounts offices. It is possible to form a general idea of their organization from what was said in the chapter on Financial Structure and the frequent reference to the function of the Audit and Accounts Officers in other chapters. But it will serve some purpose if the whole information is brought to a focus, more so because a clear understanding of the position and duties of these officers is necessary for following the arguments elaborated in the next paragraph. The most distinctive feature of their work is the combination of the audit and accounts functions, and the fact that the Auditor-General is responsible for the efficient discharge of both. He is a statutory officer, his appointment being regulated by the provisions of Section 96(D) of the Govern-

ment of India Act, and his powers, duties, and conditions of employment defined in the Auditor-General's Rules framed under the same section.[1] He is the head of all accounts and audit offices except those that deal with military accounts, and is responsible for the conduct of business, administration, organization, and the maintenance of discipline. He is to see that the audit is conducted with reference to the canons of financial propriety, and the cases of the breach of any one of them is brought to the notice of the Government either by himself or by the other Audit Officers. He can be required to arrange for the audit of accounts of the Revenue Department, or that of the store and stock on behalf of the Government. He is empowered to order the recovery of the amounts placed under objection unless the Government obtains the requisite sanction, undertakes to report the irregularity together with the action taken by it to the Public Accounts Committee. He is to obtain the Appropriation and Audit Reports from the Audit Officers and forward them to the Government concerned, and through the Governor-General in Council to the Secretary of State with his detailed comments on each report. He can call for any documents, papers, or books relating to accounts for inspection unless the documents in question are certified as confidential, in which case he or the other Audit Officers are to accept an authenticated statement containing the required facts and figures as correct. The audit of sanctions accorded by the Governor-General in Council is under his immediate supervision. The doubtful or disputed cases of audit are referred to him for decision against which there is no appeal. In matters relating to accounts he possesses similar powers. The form in which the accounts are to be kept and rendered is determined by him, and no change can be made in the nomenclature or the order of major or minor heads without his sanction. All doubts or disputes regarding classification of transactions are finally settled by him. He is to compile the

[1] An extract from these rules is given in Appendix VIII.

consolidated accounts of India and submit them to the Secretary of State of India. He and Audit Officers have to furnish information to the Government which can be derived from the accounts maintained in the offices under the control of the Auditor-General, and render assistance in preparation of annual budget estimates. He, in his turn, can require any Government Officer to supply any information needed for the completion of accounts to be submitted to the Secretary of State. He can inspect personally or through his Deputy Auditor-General any office of audit or accounts. He is appointed by the Secretary of State in Council and is not eligible for any other office under the Crown on vacating his office. Though independent of the Government in matters of audit, he, as the head of the Indian Audit Department, is under the administrative control of the Finance Department of the Government. He checks the work of the audit offices through his two Deputy Auditors-General, who visit different account centres for this purpose. There is an officer styled as the Auditor of the Government of India Sanctions who examines all sanctions accorded by the Government of India except those pertaining to railways, which are audited by the Accountant-General, Railways. Actual audit and account work is done by four classes of officers, viz.: Civil, Military, Railways, and Posts and Telegraphs. The civil offices of audit and accounts, besides dealing with the accounts of the civil departments, classify, audit and compile the accounts of the Forest and the Public Works Departments. The Accountant-General, Central Revenues, maintains and audits the accounts of the Central Government and the minor administrations working directly under it. In every Governor's province there is an Accountant-General who performs the same duty for the Provincial Government. The accounts connected with the agency functions of the Provincial Governments are also dealt with by the same officers. In Assam the highest Audit Officer is designated as the Comptroller, but performs the same duties as the Accountants-General. The

Accountants-General are the officers of the Central Government, though in matters of audit they are only responsible to the Auditor-General. The military accounts are in charge of the officers of the Military Accounts Department, who are under the administrative control of the Military Accountant-General. The latter officer works under the direction of the Financial Adviser, Military Finance, who has been already stated, is an officer of the Finance Department. The military administration is divided into four commands, each one of which is subdivided into districts. There are fourteen military districts in all, and in each district there is an Audit Officer called the Controller of Military Accounts. The Controller of Military Accounts, whose head-quarters are located at the Head-quarters of the Command, is the chief authority for the accounts and internal audit of the Command, and can set aside the decisions of the other Audit Officers. The Controller of Military Accounts, besides being the Audit and Accounts Officer, is also the Disbursing Officer of the district. He makes payments by cheques drawn against the letters-of-credit. The accounts of the Royal Air Force, Army Factories, and Marine are dealt with by separate Controllers of Military Accounts, who perform the same functions. The Accountant-General, Railways, is the head of the Railway Accounts Offices. He supervises the work of the officers in charge of accounts of the State-managed railways, and of those who are attached to the Company-managed railways for safeguarding the interests of the State.[1] The Audit Officers of the Railways also make payments after the pre-audit of bills through the agency of a staff of travelling pay clerks. The Accountant-

[1] In the following directions there is the necessity of exercising a close check and supervision :

(1) To ensure the proper upkeep and maintenance of the railway, so that, on termination of the contract, it may be handed back in as good condition as when it was made over to the Company.

(2) To examine all proposals for fresh expenditure of capital and check any tendency to extravagance in that direction.

(3) To watch the proper application of funds to Capital purposes for improvements, and to Revenue purposes for upkeep and maintenance.

(4) To verify the correctness of accounts and of the division of profits.

General, Posts and Telegraphs, is in charge of the accounts of Posts and Telegraphs Department. He has six Audit Officers under him, four for postal and two telegraph.

The status of the Auditor-General has been raised by the Reforms. The difference between his present position and that which he occupied before the Reforms is not so great as to change its fundamental character. Before the Reforms he was nominated by the Government of India, but his appointment was subject to the approval of the Secretary of State. Then he was an officer of the Government of India and subject to the same conditions as the other public servants. Now a provision has been made for his appointment in the Government of India Act, which, as stated in the foregoing paragraph, is made by the Secretary of State in Council. Sir Malcolm Hailey, referring to the change that has taken place in his position, said in one of his speeches in the Legislative Assembly: "We have now an Auditor-General who is an independent authority. His position is recognized in the Government of India Act. He is, I say, independent of the Executive Government. He is an official interpreter to us of the orders of the Secretary of State, and he is an authority whose verdict we never venture to call in question." These words were used with a view to convey the inference that the Indian audit is completely independent and can be relied upon for maintaining order, economy, and regularity in the financial administration of the State. It is necessary to understand the position clearly in order to judge the correctness of this inference. In this connection we have to take into account two considerations which have an important bearing on the question. The Auditor-General and his Audit Officers have been assured a position of independence in matters relating to audit. In the pre-Reform days also the audit decisions of the Auditor-General could not be challenged by any authority in India. But the Auditor-General, besides being the chief auditor of the realm, is also the highest accounts officer. The officers under him also combine the audit and the accounts

functions. The military and the railway Audit Officers, who between themselves are responsible for the audit of more than half the expenditure of the Government, are also the paymasters of their departments as well. The accounts and disbursing functions are essentially executive functions, in the discharge of which the officers concerned must be under the Executive Government. The science of psychology has not sufficiently advanced to assert the possibility of two distinct personalities residing in the same official vehicle, and acting independently of each other. The public servants cannot play the interesting rôle of Dr. Jekyll and Mr. Hyde in their official capacity. The official personality cannot be split into two parts, one being independent of the Executive and the other subordinate to it.[1] Any contentions to the contrary and the frequent use of the categorical imperative cannot change this obvious fact. The other consideration which can be urged in this connection is that the assumption that the Executive Government means the Government of India, is against the fundamental basis of the Indian constitution and the known facts. In theory as well as in practice the Secretary of State is supreme in the Indian administration. In matters of finance he performs duties which are not insignificant in any sense of the word. The proposals relating to changes in the

[1] The Auditor-General himself has pointed out this difficulty in his Note on Audit and the Accounts under Reform Scheme. He says: "It is of the utmost importance that an audit officer should be in as independent a position as possible. There cannot be complete independence of audit in India so long as the Accountants-General, who are responsible for the initial audit, are directly subordinate to the Government of India, seeing that some orders, which they have to apply in audit, are orders issued by the Secretary of State defining and limiting the powers of the Government of India. It is no answer to this argument to say that the supreme audit authority is vested in the Auditor-General, because the Accountant-General is responsible for framing his own conclusions as to the sanction required for any item of expenditure, and the intervention of the Auditor-General is secured only by way of appeal against his decisions. Again, it cannot be said that the Auditor-General is in complete independence so long as the position is that the officer, who as Auditor-General is supreme in audit matters, is, at the same time, subordinate as Comptroller-General to the Government of India in the administration of the department."

The Auditor-General as the head of the Audit Department is under the Finance Department of the Government of India.

rates of taxation, creation of highly paid posts, expenditure of large sums on railways, irrigation, and other projects entailing heavy outlays, and the raising of loans, as a matter of fact any important departures from the existing state of things cannot be given effect to or placed before the Legislature without his previous sanction. These remarks are also applicable to the Provincial Governments with this difference, that they can, within certain limits, vary the rate of taxation or impose new ones without his sanction. This is so in theory, and if the testimony of those who have got an inside knowledge of the working of the Government of India Act is to be depended upon, also in fact. It is the Secretary of State who is the responsible head of the Indian Treasury and the Finance Members of the Central and the Provincial Governments are his agents. It is idle to contend that the Auditor-General is independent of the Executive, when he is appointed by and responsible to the Secretary of State. He is under the Chief Executive, who is nominally responsible to the British Parliament but in reality his own master. The Finance Members are in a way the central figures in the finance of the country. They are the financial experts, prepare estimates, and, as the spokesmen of the Government, have to controvert the arguments of the non-official members in the budget and the other debates. But that does not in any way affect their subordinate position. They are what they are in spite of the fact that they appear in the rôles of the Chancellors of Exchequer in the financial dramas that are played before the public gaze every year. The vital problem of the audit control is the necessity of imposing some check on the whole body of the Indian Executive. It is not enough to audit the accounts of the subordinate officials by an agency independent of their control. The pre-Reform system was effective for the maintenance of official discipline and day to day audit. The India Office was the authority on which it was necessary to impose some audit restrictions. The Reforms have not supplied that deficiency. Audit is no more independent now than before.

The necessity of making it quite independent is now admitted. There are two ways in which that can be done. One of them is more important than the other, and also practicable, but not very useful. The other, though less important of the two, is both practicable and useful. The Auditor-General and the Audit Officers can be independent of the Secretary of State in Council. This can be done. There is no insuperable constitutional difficulty in the way. The Auditor of Indian Accounts has, since 1858, been independent of the Secretary of State without the Indian constitution, such as it was, and is, falling to pieces. The Auditor-General can be assigned a similar position without any "cataclysmic" changes. But unfortunately that cannot take us very far. The Auditor-General under the present constitution cannot be made responsible to the Indian Legislature. He must, if at all, be a servant of the British Parliament, but as it neither grants funds nor examines the Appropriation Accounts to see how they have been spent, the responsibility of the Auditor-General to the British Parliament cannot improve matters. His Appropriation Report can, of course, be duly laid before the two Houses of Parliament, but as a constitutional check this ceremony can be of no value. And it is too late to suggest that the Parliament should grant supplies and examine accounts. The events have gone too far to make that even thinkable. The other measure is not as futile, though less important. It is that the Audit Officers should be relieved of their accounts and other duties and made exclusively responsible for the audit of accounts. There are other reasons why a complete separation of accounts and audit is desirable. The Inchcape Committee has advocated it on the ground that the Provincial Governments can require the Accountants-General to furnish information which can be derived from the accounts and render assistance in the preparation of the annual estimates, and thereby throw work on them entailing extra expenditure for which they have no responsibility. That, of course, means that the Provincial Accounts should be

maintained by an agency controlled and paid by the Provincial Governments. This aspect of the question has been dealt with in the preceding chapter. The other argument in favour of the same measure has also been referred to. It is necessary to separate audit and accounts for it is desirable to make the Finance Department responsible for the determination of the form of both the estimates and the accounts to ensure correspondence between the two. But the reason with which we are here primarily concerned is, that the combination of the audit and accounts functions is incongruous on account of the need of making the former a discreet quantity. "They are," to quote the words of Lord Welby and his two colleagues, "in their nature distinct and ought to be kept distinct." Lord Welby and his colleagues had, in laying down this principle, a number of other executive functions in mind, the control of which is now vested in the Controller of Currency. The Auditor-General was, besides audit and accounts, responsible for ways and means programme, resource operations, management of balances, public debt, and paper currency system. He was relieved of these functions when the post of the Controller of Currency was created in 1914. The Provincial Accountants-General, who continued to be in charge of the currency and resource work till 1920, were relieved of these duties when the Reforms were introduced. The evolution of the Audit Officers has, till now, been in the direction of greater specialization. It is necessary to take a step further and bring about a complete separation of audit and accounts duties.[1] This measure of financial reform will clarify the

[1] From the evidence given by Sir F. Gauntlet, before the Reforms Enquiry Committee, it appears that the question of the separation of the audit and accounts functions is engaging the attention of the Government of India. We are told that if the regulations regarding the pre-audit of a certain class of bills are not enforced, the reform can be carried out.

Mr. Jukes, of the Finance Department, in his Memorandum prepared for the Reforms Enquiry Committee recommends the separation of audit and accounts in the interest of fuller financial autonomy of the provinces. He says: "It is, of course, true that the fact that its accounts are compiled for it by an independent and highly competent agency constitutes, in practice, no serious restriction upon the autonomy of the local

issues, and give to the Audit Officers a certain amount of aloofness which they ought to have but do not possess. But it will not give us a system of independent audit. For that, we must wait till India has attained the status of a self-governing nation. It is not a very hopeful conclusion to have to come to, but is in accord with the facts of the case. It is certainly better than believing in the efficacy of a check which is illusory and can only create a false sense of security.

Government. In theory, however, such a situation is entirely inconsistent with any real degree of financial independence. It is almost an axiom that an authority which is responsible for the expenditure of considerable sums of money should also be responsible for accounting for that expenditure. Its autonomy must remain in a very rudimentary stage as long as it has no sort of control over the agency which compiles its accounts. It is, therefore, represented that, if any advance in the financial autonomy of the provinces is to be made, the first step should be to transfer to the Local Government the responsibility of maintaining their own accounts. This would, of course, mean that the Local Governments must in future relieve the Central Government of the cost of compilation. The change would require no amendment of the statutory rules beyond the change in Item 15 of the Part I of the Schedule I of the Devolution Rules and the alteration of the several of the Auditor-General's Rules under Section 96 D(1)."—*Vide* Appendix V to the Reforms Enquiry Report, page 443, par. 11(1).

The Legislative Assembly has, since the above was written, accepted the proposal of the Government of India for the separation of audit and accounts on the East India Railway as an experimental measure. In future the Auditor-General will only be responsible for the audit, and the control of the accounts of the railways will pass on to the Financial Commissioner of Railways.

CHAPTER XII

PUBLIC DEBT

The public debts have, almost in all countries, assumed an importance in their financial organization which makes their management a matter that calls for the exercise of skill, foresight, and understanding. They are incurred either to meet temporary or exceptional emergencies, and the expenditure involved in the public works of remunerative and non-remunerative character. Their effects on national life vary according to their objects, magnitude, terms of payment of interest and repayment of principal, and the class and the nationality of the public creditors. It is not necessary to analyse all their effects and point out the way in which they are related to one another. But it is important to remember that of all the problems which require careful handling on the part of financiers, the management of public debts is not the least important. The disturbing effects of public debts which various countries have accumulated during the war have become a matter of common knowledge, and it is admitted that without the settlement of this question it is not possible to find a satisfactory solution of the international difficulties. In India the position is a great deal better than in other countries, and the problem does not require immediate attention. The need of vigilant care, however, in watching the growth of public debts or providing safeguards against the measures which will ultimately recoil on the financial stability of the country is not less urgent on that account. The temptation of meeting the expenditure out of loans, which ought to be charged to the annual revenues, is always strong. In a country in which

the taxable capacity of people is limited and the public needs, that are clamouring for satisfaction, numerous, every expenditure from loans is likely to appear in the light of investment, which promises rich return in the near future. If the money for education, public health, and various demands of national life is found out of borrowed funds, it will not strain the resources of the taxpayer, and give us services which are admitted to be necessary and beneficial. But if it becomes part of our accepted financial policy to defray the expenses of such activities from public loans, the door is opened for the use of devices which have everywhere led to financial disorganization. It is not suggested that on no account should the loans be used for the introduction of compulsory elementary education, improvement of sanitary conditions of the masses, or other schemes of the same kind. It may, under certain circumstances, be the only feasible course, and when the object of expenditure is one which cannot on account of its importance from the national standpoint, be put off, it may perhaps be also a desirable course. But it has to be remembered that use of loans for such purposes is attended with very grave risks, and the presumption against it is so strong as to require exceptional circumstances for its justification. It may be preferable to go a little slow in realizing these pre-eminently desirable ends rather than to adopt the path of least resistance. The unwarranted use of loans is also to be deprecated for another reason. The taxpayers and their representatives are a little less careful in the scrutiny of the proposals which do not touch their pockets immediately. The schemes which would not pass muster on closer examination are got through the Legislatures without much difficulty because they are not accompanied by proposals for fresh taxation. In this way all kinds of proposals of doubtful utility receive the sanction of the Legislatures which would, otherwise, have rightly been nipped in the bud. The consideration has special importance for a country in which the democratic control of public finances is just beginning and has not been estab-

lished. The Executive Government can, by resorting to loans, evade the vigilance of the Legislatures, and smuggle through unnecessary or extravagant schemes of public expenditure. It has been considered necessary to emphasize the disadvantages of the use of loans because of the scant attention which they have received in the past. The summary way in which the demands for the grant of money for railway expenditure have been disposed of in the last four years by the Legislative Assembly is partly to be attributed to the public indifference to matters relating to public debts. In one province[1] at least a loan has been floated for financing schemes which it may be assumed would not have been undertaken if the total or a part of outlay had to be met from the yield of taxes. The situation is not serious, and the mistakes that have been committed can be rectified. But it is necessary to bear its possibilities in mind. The motto that "the evil that men do, lives after them" is, as Dr. Dalton has pointed out, specially applicable to the public loans for purposes other than those for which they may or must be used. With this general consideration in mind, the study of the technical aspect of the management can now be undertaken.

The public debts can be classified in different ways. One differentia for the purpose is the time of the repayment of loans. The debt which is repayable within a year of the time that it is incurred is called floating or "unfunded" debt. The co-relative of "unfunded" is "funded," which adjective is applied to public debt when the Government is not under the obligation to repay the principal, or has to do so after a certain number of years. The distinction is somewhat arbitrary, for there is no reason why the loans

[1] The United Provinces Government floated "The United Provinces Development Loan" which yielded 4,19,42,000. The loan funds were used for purposes which, in the opinion of the local Accountant-General, could not come under the objects for which the borrowing of money is allowed under the rules. The proceeds of the Development Loan have been partly expended for purposes some of which may be described as indirectly productive by giving a free play to our imagination, but which neither directly nor indirectly can contribute to the development of the province.

which are technically outstanding for a few months, but can be renewed with great ease, should be called "unfunded," while others which mature in three or five years and then have to be liquadated are called "funded." A number of Governments make their floating debts run for quite a long period by renewing the old obligations and make them a part of their permanent debt which they choose to keep suspended in a floating form. But the distinction, though a little vague, is useful. When a Government cannot repay its short-dated obligations on maturity, it is always wise to convert them into long-dated obligations, or, to use the common phrase, to "fund" them. The other basis of classification is to differentiate them according as they are or are not "productive." The productive debt is fully covered by assets which are expected to yield a sufficient income to pay interest on the debt and a certain rate of profits, the unproductive debt being a dead-weight burden on the resources of the State. A loan, the proceeds of which are spent for purposes which are not directly remunerative, but which may be calculated to increase the economic resources of the country by improving the intellectual or the physical capacity of the people, does not become productive on that account. Public debt may also be external or internal, that part of the debt which is in the hands of the citizens of a State being considered as "internal" and the other which is held by aliens as "external." The political, economic, and social consequences of the external loans are essentially different from those of the internal loans, and the distinction is, on that account, real and important. Public debts can also be distinguished according to the authorities that raise the loans. Our debt is either "central" or "provincial" according as the loans are borrowed by the Central or the Provincial Governments.

The total public debt of India on the 31st March, 1924, was 905·65 crores. Of this, 740·03 crores represent the funded and 75·48 crores unfunded debt. The balance of 90·14 crores represents the amount due on account of the

Terminable Railway Annuities—an obligation the nature of which will be explained a little later. Here it is enough to say that this is an obligation which cannot fall under the category of floating debt, but is also not quite like the funded debt. Taking the second differentia, the total debt of 905·65 crores is composed of 578·39 crores of productive and 228·45 crores of unproductive debt.[1] There is a balance of 98·81 crores which is represented by loans to Provincial Governments. Analysing the funded debt, according as the debt is registered in India or in England, the amount is composed of 358·79 crores in India and 393·12 crores in England. Of the debt registered in England, which is calculated in sterling and the interest on which is payable in sterling, the whole amount is practically in the hands of the English investors. This part of the public debt is known as the Sterling Debt. The debt registered in India is called the Rupee Debt[2], as it has been subscribed in rupees, the interest due on it is payable in rupees, and the principal when repayable, is also paid in rupees. The bulk of this debt is held in India, but a certain portion of it is also in the hands of investors who live in England and draw interest due to them in that country. Of the rupee debt held in India a part is in the hands of the Indian investors and the other is held by the European investors. In order to find out what proportion of debt is external, it is suggested that all debt, whether rupee or sterling, held in India or in England, which is in the hands of the non-Indians should be treated as external, and rupee debt in the hands of the Indians as internal. This basis is suggested not on account of any racial bias or political prejudice. The Indian debt held by the non-Indians is external, because its economic effects are analogous to the effects of the external loans. The

[1] It may be added that with the exception of a certain amount of specific Railway debt no distinction has been made in the accounts between the loans raised by the Secretary of State or the Governor-General in Council for productive or unproductive purposes.

[2] The Rupee Loans, like the Sterling Loans, are issued in the name of the Secretary of State in Council.

interest paid on this amount and the repayment of the principle may be taken as a transfer of wealth or its equivalent value from India to England. Part of the amount paid to the European investors in India may be spent here, and, therefore, constitute transfer of wealth within the country. But broadly speaking, the assumption that the investment of funds by the European investors in the Indian loans means in the first instance transfer of wealth from other countries—chiefly England—to India, and then from India to foreign countries—again chiefly England—is correct. The figures of the amount of the rupee debt outstanding in the hands of the Europeans in India and in England on the 31st March, 1924, are not available, but if we take the proportion of the rupee debt held by the Europeans and the Indians seven years ago, in 1917, we find that in that year, of the total rupee debt of 202·15 crores, the Indians held about 101·75 crores and the Europeans 100·4 crores, or roughly speaking we may say that the rupee debt was shared equally between the Europeans and the Indians. During the seven years the proportion is likely to have changed in favour of the Indians, as the Government loans have of late been growing in popularity with the Indian investors, but the difference cannot be appreciable. Taking it for granted, therefore, that 50 per cent of the rupee debt is in the hands of the Europeans, the external debt of India, adding half of the rupee debt to the total sterling debt, amounts to 77 per cent of the total funded debt. As for the unfunded debt it is not possible to work out the proportion between the Europeans and the Indians. The analysis of the figures brings out two features of our public debt, both of which are important. One is that the unproductive portion of our public debt is much smaller than the productive debt. This is, it need not be added, a gratifying feature of the Indian debt. Very few countries are in a position of possessing valuable assets, which India possesses, as a cover for about 75 per cent of her public debt. This is an enviable position on which we can well congratulate

ourselves. In other countries the public debts are the financial mementoes of the wars in which they took part or were embroiled. Their reduction is one of the most serious problems with which they are confronted. The redemption levies, cancellation of international debts, even repudiation and various other measures have been suggested for easing the situation. India's unproductive debt has also increased on account of the war and its aftermath. In 1917 our unproductive debt, or the ordinary debt, as it is called, would have been practically extinguished. But on account of the war contribution and five years of continuous deficit, India has again 228·45 crores of unproductive debt to pay off. But still the position is not unsatisfactory, and if it is not allowed to become worse, it need not cause any anxiety. The other feature of our public debt—the preponderance of the aliens among our public creditors—is not as reassuring. The fact that the Indians have not invested more freely in the public loans is their own fault. It is due to the limitation of their resources and absence of investing habits. But the fact, whatever its explanation, is disquieting in itself. As this aspect of the question is further considered in the concluding paragraph of this chapter no more need be said about it here.

The funded debt can be further sub-divided into terminable and interminable debt. The part of the public debt, the principal of which need not be repaid, is called interminable, as it can remain outstanding for an indefinite period. The Government has, however, got the option of paying it off at a short notice, if it finds that it can do so either out of surplus revenues or funds borrowed at more favourable rates than those payable for the outstanding loans. The terminable debt, as its name indicates, has to be liquidated after a specified period, though in some cases the creditors are guaranteed against the repayment of the loans before the expiry of another specified period. This guarantee is also sometimes given to the investors of the interminable loans. The terminable loans are, at times,

issued at a discount or the amount subscribed is less than the face value of the loan at which it is to be redeemed. The use of this device enables the Government to reduce the nominal rate of interest on the loans, for, from the point of view of investors, it is immaterial whether they get 4 per cent for the loan, the nominal value of which is Rs.100, but for which they have got to subscribe Rs.80, or 5 per cent for the loans, the nominal value of which is equal to its real value, i.e. which is issued at par. The Government gets relief in the immediate future, for the amount which the Government has to pay on account of its interest is in this way reduced, though the liability when it matures is much heavier, for the debt has to be redeemed at the face value of the loan. The other inducement which the Government holds out to the investors is to exempt interest payable on the loans from the payment of the income-tax. The issuing of loans below par, making them income-tax free, or the use of similar other devices is necessary when the Government is hard pressed for money and desires to tap new sources for its loans. The loans issued before the war were all interminable, which, as already stated, does not debar the Government from repaying them, if it can do so with advantage. The loans issued during and after the war are terminable and some of them have been issued at a discount and are income-tax free.[1] The terminable annuities are an amphibious portion of the public debt, which is neither floating nor fixed. The Government, when it bought the railways, which are now State property, did not, in some cases, raise loans for the purpose. It bought them on credit and has since been paying off the amount by a series of *equated* payments, each instalment being made up of (*a*) a part payment in discharge of the liability, (*b*) interest for the credit given. With the passage of time the liability has been reduced, and portion of payment representing interest has been diminished and the portion representing the discharge of liability increased.

[1] The particulars of the loans outstanding on the 31st March, 1922, are given in a note.

In 1958, when the period for which the annuities have to be paid, expires, the State will become the owner of the railways, to which there will be no encumbrances attached. The fact that part of the liability matures every year makes the terminable annuities like the floating debt and the fact that the liability remains outstanding for a number of years makes them analogous to the funded debt. But they are neither one nor the other. The unfunded debt has a number of constituents. The first in order of precedence come the treasury bills. The legitimate purpose, for which they can be issued, is when the income from taxes, etc., falls short of the amount needed to meet the current expenditure. This is the method by which the Government discounts its assured revenue. A treasury bill is like a commercial bill of exchange which comes into existence because those who have got claims on the proceeds of the sale of goods on their way to consumers, want to anticipate the payment of fund which in the ordinary course of trade is sure to arise. The treasury bills are the means by which the Government anticipates its specific income. The revenue is expected to come to hand later in the year, but as the Government needs funds before it is realized, it borrows money for a short time in order to tide over the temporary deficiency. The treasury bills have a currency of three to twelve months. They are issued at a discount, which, of course, means that the amount subscribed is less than the face value of the bill, the difference representing the yield of the investment. There are two ways in which the treasury bills can be issued. One is to invite competitive tenders from the investors who offer the price they are prepared to pay for the bills and specify their total investment. The investors calculate the price by deducting from the amount that they will receive on the maturity of the bills a certain percentage as interest on the amount they advance during the currency of the bill. The rate is fixed by the tenderers and is determined by the state of the market for short loans at the time that the tender is made. The other method is to fix the price at which the bills will

be sold, and invite subscriptions. The Government in fixing the price takes the state of money market into account and calculates the rate of interest at which the requisite amount can be raised, deducts the corresponding amount from the face value of the bills and then offers them for sale. The experience shows that the Government obtains better rates by a tender system judiciously worked, than by sale at fixed rates. It has already been stated that the governments of a number of countries have often committed the mistake of renewing the bills on maturity, instead of discharging them, and have thereby made the treasury bills a part of their permanent debt. The Government of India began to make use of the treasury bills in 1918, when on account of the difficulties created by the war the Government had to find money for payments on behalf of the Imperial Government. But since then it has made use of them not only to anticipate its assured revenues but also to meet its recurring obligations. At one time the total amount of the treasury bills in the hands of the public reached a very high figure,[1] but on the 31st March, 1924, the outstanding treasury bills were valued at 2·13 crores. The reduction has been brought about by discharging the treasury bills from the proceeds of long-term loans. It is a bad policy to increase or even renew the floating debt from year to year, as its effects on the economic life, which need not be explained in detail, are undesirable. The Government of India also gets over its temporary deficiency of revenues by taking advances from the Imperial Bank and repaying them after a few weeks. These loans are called Ways and Means Advances. It may be mentioned in the passing that as now the Government can depend upon the sale of the treasury bills and advances from the Imperial Bank for replenishing its treasury balances, it is not necessary to maintain them at the high figure, below which it was considered unsafe to reduce them before the war. The other constituents of the

[1] On the 31st March, 1922, the value of the treasury bills in the hands of the public amounted to Rs.53,96,70,000.

unfunded debt are the Post Office Cash Certificates, Postal Savings Bank Deposits, and a number of other miscellaneous obligations. The Post Office Cash Certificates, like the treasury bills, were introduced during the war in order to reach the smaller investors for raising public loans. They have since become a permanent feature of the loan policy of the Government. They are sold at less than their face value[1] and have a currency of five years, at the expiry of which they are repaid. The special attraction of the Cash Certificates is that the investor's money is not necessarily locked up for the full term of five years, for he can obtain payment at any time during the currency of the certificates and receive an amount which is higher than the original purchase price, according to the period during which he has held the certificate. These certificates are for sale all the year round and can be obtained at every important post office. On the 31st March, 1924, the certificates to the extent of 8·51 crores were outstanding in the hands of the public. The sale of Cash Certificates has, besides bringing money into the treasury, the advantage of stimulating investing habits and encouraging saving among the people of small incomes. It is not necessary to explain why the Cash Certificates have been classed as the floating debt. They remain outstanding for five years, but since payment for them can be obtained at any time during their currency, they are like the loans at call, which the banks can recover without any notice. They have, as a matter of fact, been called the interest-bearing currency notes. The Postal Savings Bank Deposits do not require any explanation. A sum of about 25 crores is held by the Government on this account, which the Government is liable to repay without any notice. The balance of about 40 crores of the unfunded debt of the Government of India is represented by a number of miscellaneous obligations, which need not be detailed here. This paragraph, which is

[1] They are issued in the denominations of Rs.10, 20, 50, 100, and 500 on payment of Rs.7·12, 15·8, 38·12, 77·8, 387·8 respectively. The yield to the investors ranges from 4 to $5\frac{1}{4}$ per cent if held for the full term of five years.

unavoidably full of so many figures, may be concluded by referring to one or two considerations of general importance. The rupee debt of India has since 31st March, 1914, risen from 146 crores to 358·79 crores on the 31st March, 1924, while the corresponding figures for the sterling debt are £177 millions and £260 millions. The increase in the rupee debt is about 150 per cent, and the increase in the sterling debt is about 50 per cent. As the bulk of the rupee debt is subscribed in India, the growth of rupee debt is the sign of the growing dependence of India on her own resources for her capital requirements. Before the war the maximum amount raised in India was 4½ crores. During the war the public loans yielded about 50 crores in the years 1917 and 1918, and even making allowance for the fact that special campaigns had to be organized for this purpose and that the whole official machinery set in motion for getting money from the investing public, these amounts are very large compared to the pre-war figures. The amounts raised in the subsequent years have also been considerable. In 1922–23 the subscription to the rupee loan amounted to 47 crores out of which only 65 lacs were received in London. In 1923–24 the rupee loan yielded about 23 crores. India will still for some time to come depend upon foreign resources for raising the necessary loans, but these figures clearly show that the investing possibilities of India have not yet been fully exploited, and if the banking system is properly organized, much larger funds can be raised in the country than has been done in the past. The other feature of the rupee loans is the increase in the number of investors. Formerly the loans were practically subscribed by the merchant princes of the presidency towns, and the investors of the country at large did not take to them very favourably. Now the number of the investors has very greatly increased, and the arrangements have been made for the payment of interest and a number of other matters connected with the administration of the public debt at the treasuries and the sub-treasuries, the officers in charge of which have been instructed to put

through the business of the investors with expedition and treat them with utmost consideration when they have to visit the treasuries in connection with their investments.

The funded debt of India is held mainly in three forms: (1) the Stock or Book debt as it is sometimes called, (2) Bearer Bonds, (3) Promissory Notes. When the debt is held in the form of stock, the owner is given a certificate that he has been registered as the proprietor of a certain amount of Government stock in the books of the Public Debt Office. The certificate is called the Stock Certificate, and the ownership of the Government stock depends not on the possession of the certificate, but on the fact that the owner's name is registered in the books of the Public Debt Office. The change of ownership can be effected by two parties filling a printed form before a witness. The owner of the certificate possesses complete security against theft or the loss of the certificate in some other way. The interest on the Government stock is paid on warrants which can be drawn on any treasury or sub-treasury. The bearer bonds, as their name indicates, are payable to the bearer and as far as the Government is concerned, the possession is sufficient proof of their ownership. There are interest coupons attached to each bond, and the payment is made to the presenter of the coupon on the due dates at the Public Debt Office or at any treasury or sub-treasury at which the bond is registered for the payment of coupons. The absolute freedom with which the bond can change hands is its chief advantage. It, of course, makes the safe custody of bonds a matter of special importance, but those investors who can make the necessary arrangements for this purpose, and want to keep their assets in a readily negotiable form prefer to hold their investments in the bearer bonds. A promissory note can be disposed of by the owner by making an endorsement in favour of the buyer at the back of the note. The interest is payable at any treasury or sub-treasury at the option of the holder. It is paid by the presentation of the note itself. A promissory note is more secure than a bearer bond but not as

secure as the stock certificate. Stock certificates and the promissory notes are issued in respect of any loan and of any denomination subject to the condition that it must be a multiple of Rs.100. Bearer bonds are issued in respect of three loans and are of the denominations of Rs. 100, 500, 1000, 5000, 25,000. It is possible to convert one form of security into another.

Sir Basil Blacket, in his Budget speech of 1924, outlined a scheme which, in his opinion, should be adopted for the discharge of public debt. He wanted to provide for the extinction of our entire public debt in 80 years, of our war debt of 120 crores in 50 years, of the debt of 98 crores due to the accumulated deficits of 5 years ending 31st March, 1924, in 25 years, and of the debt of 9·85 crores due to the construction of New Delhi in 15 years. He laid special stress on the adoption of a programme of debt redemption based on stable and well-considered principles. The question is very important and has not received the amount of attention that it deserves. The Government of India has utilized considerable sums in the past out of its annual revenues for the reduction of debt. The payment of railway annuities is an obligatory charge which it has been meeting from its railway revenues. The initial liability which has been undergoing redemption in this way was about 123 crores, out of which about a sum of 30 crores has been discharged by the end of the year 1922–23. Besides the discharge of debt by annuities the Government has been redeeming the India Stock for which the shareholders of railways were in some cases permitted to exchange their annuities and the securities of the original companies from which the railways were purchased. The liability thus discharged has been appearing under the head Sinking Fund, and out of the initial liability of about 19·5 crores about 10·5 crores has been discharged by the end of the year 1922–23. The Government of India has, besides making this provision for repayment of the railway debt, undertaken to set aside 1½ per cent of the total amount of 5 per cent War Loan of 1917 for the purchase of the

securities of the loans, whenever the market price falls below 95, at which price the loan was issued. As the market value of this loan has depreciated since its issue, the provision has to be made for the purchase and cancellation of its securities. The Government of India steadily pursued the policy of utilizing its revenue surpluses for productive expenditure. The sums could have been used for the purchase of outstanding loans, but as the Government of India was borrowing heavily for its capital requirements, there would have been no sense in raising loans with one hand, and repaying the old ones with the other. The surplus was, therefore, rightly used for the extension of railways and irrigation facilities, and the amount thus spent charged to the capital account of the productive enterprises concerned. The necessary adjustment was made by increasing the productive debt and reducing the unproductive debt referred to in the foregoing paragraph, the extinction of which was well within sight in 1915–16, and was the result of this policy. The unproductive debt was 105 crores in 1900 and was reduced to 3 crores in 1915–16. The amounts spent by the Government of India for debt redemption would thus appear to be considerable. The complaint is not that the Government of India has not done anything for the reduction of debt, but that it has not been guided by any consistent and well-recognized policy in this matter. It is now necessary to adopt some stable policy. The debt discharged till now has been extinguished more or less as a result of a series of accidents. The first principle, which can be enunciated in this connection, is that the debt must be discharged out of the revenues, unless the new loans in repayment of the old loans can be raised at a lower rate of interest, in which the conversion of securities bearing a high rate of interest into others for which the annual charge on account of interest is less justifiable. This is the only way the debt can and ought to be reduced. The Government of India has, since 1918, in spite of heavy deficits and large borrowings at a high rate, been providing money for the payment of railway annuities, sinking-fund charges,

purchase, and cancellation of 5 per cent loans and the discharge of $5\frac{1}{2}$ per cent war bonds. The interest paid for the new loans has been generally 6 per cent and even more. The policy, which on account of the existence of the contractual obligations and maturing of the 5 per cent bonds has been forced upon the Government of India, is essentially wrong. It is bad finance to borrow for the payment of old debt at a rate higher than that which was being paid for the redeemed liability. From this point of view, the purchase of railways under the annuity system, or by the issue of the India stock, to which an obligatory sinking-fund provision is attached, is to be deprecated. The right method is to issue interminable loans for the purchase of railways, the interest of which should be charged to their annual revenues. The liability undertaken by the Government of India for the cancellation of 5 per cent war loans in case of the depreciation of the securities is open to objection on the same ground. The use of 5 and 10 years' bonds, which were employed to such a large extent during the war, and the maturing of which has been a source of embarrassment, is also an unsound expedient for the same reason, unless the loans are raised for incurring some expenditure which ought to be met out of the revenues of the country but which on account of its magnitude cannot be so met. They had to be used during the war, because probably otherwise it would have been impossible to float large war loans, but there is no justification for the continued issue of the Government loans in this form. The public loans should either be interminable or, if terminable, should be payable at a date quite distant from the year of their issue, the Government, of course, reserving to itself the right of repaying them at any time if it can do so without detriment to its more important interests. This is the only way in which the springs of national economy can have free play and room for unhampered movement. The arguments against making what were once known as the "inviolable appropriations" or contracting obligatory liabilities for the redemption of debt cannot be urged against evolving a

systematic policy for the same purpose. It is necessary to redeem public debt, at least the unproductive portion of it, as soon as possible. As regards the redemption of productive debt there can be a difference of opinion. Sir Basil Blacket holds that it is desirable to pay it off in eighty years. It would give us very valuable, unencumbered national assets if the productive debt can be redeemed during this period. But there is a valid objection against the policy of the redemption of the productive debt. All the money that can be spared out of our annual revenues after the payment of the necessary liabilities should be utilized for the satisfaction of our vital national needs which it is admitted have been starved till now. To use the revenue surplus for the reduction of the productive debt is a short-sighted policy, when money is required for the important schemes of public welfare.[1] The productive debt can and ought to be allowed to remain outstanding. There is an undischarged liability of about £121 millions, the major part of which is to be redeemed through the operation of terminable annuities and sinking funds. It is not right to relieve the railways of the capital charge on account of the operation of these provisions. The capital portion of the annuities and the whole amount paid on account of sinking-fund charges should be transferred from unproductive to productive debt. The railways, irrigation, and other quasi-private enterprises should be debited with the whole amount of the capital outlay incurred on their account irrespective of the source from which the funds are provided, and also the full amount of interest on expenditure should be charged to their revenue account. If this principle is accepted, all future payments in discharge of the capital liabilities will reduce our ordinary public debt, and about 41 crores already paid for the same purpose should be deducted from the total amount of the out-

[1] In this connection it is edifying to recall the vigorous stand made by Mr. Gokhale in the pre-Reforms Imperial Legislative Council against the policy of using revenue surpluses for capital expenditure and indirectly for the reduction of unproductive debt. The speech delivered by him on 7th March, 1911, in which he dealt with the matter, is a model of lucidity. It will even now repay perusal.

standing unproductive debt. Our unproductive debt on 31st March, 1924, as already stated, is shown as 228·45 crores, if out of it 41 crores is deducted as suggested above the balance to be redeemed will be 185 crores. If 41 crores thus adjusted are taken in repayment of the debt of 9·85 crores on account of the new capital and that of 38·15 crores on account of the accumulated deficits our remaining unproductive debt will be composed of about 60 crores of debt due to deficits, and 120 crores to causes arising out of the war. If for the sake of the argument, the periods suggested by Sir Basil Blacket for the repayment of unproductive debt are accepted as suitable, then the war debt should be extinguished in fifty years and the debt due to deficits in twenty-five years. Basing our calculations on this assumption we ought to make a provision of about 5 crores every year for the redemption of debt. The capital portion of the annuities, payments on account of sinking-fund charges, and the provision of depreciation fund of 5 per cent loans should be deducted from the amount, before the net amount to be provided out of the annual revenues can be calculated. These charges are not fixed, but if the amounts provided for in 1923–24 are taken for the sake of illustration, we find that about the amount of 3 crores was thus provided for debt redemption, and the remaining amount to be provided out of the annual revenues comes to about 2 crores. The amount of 5 crores has been arrived at by dividing the amount of unproductive debt by fifty and the debt due to deficits by twenty-five. This is a very crude method and has been adopted for the sake of simplicity. The right method is to take a figure which, when allowed to accumulate year by year at a certain rate of compound interest, will result in the extinction of the total debt of 185 crores in the periods named above. The redemption fund, if calculated in this way, will be very much smaller than 5 crores. These figures have been given in order to illustrate the general principle which ought to be the basis of our debt-redemption policy. They may be summarized again. Debt should be redeemed

out of the surplus revenues, and, therefore, the contracting of compulsory obligations should be avoided. Our productive debt need not be redeemed so long as adequate provision is made for the depreciation of assets from the annual receipts of the quasi-commercial departments. From the unproductive debt the amount spent so far for the discharge of our capital liabilities should be deducted, and any amounts which in future will be utilized for the same purpose should be taken as having been spent for the reduction of unproductive debt. The remaining unproductive debt should be extinguished in a certain number of years. If this basis is adopted, practically very little special provision is necessary apart from the amount which has to be found for the discharge of our non-optional obligations. The position is not unsatisfactory, but it has to be regularized and placed on the basis of some well-accepted principle. The plea of Sir Basil for the adoption of a well-considered plan in this matter is unanswerable. It is possible to argue, as it has been argued, that there is no necessity for the redemption of our productive debt. It is also possible to suggest some other criteria according to which amortization of our unproductive debt should proceed. But there is no justification for the absence of policy, which has been the only policy of the Government of India till now. Now that Sir Basil Blacket has taken up the question, it is necessary that the Indian Legislature should have the position thoroughly examined, and enunciate some principle according to which the Government policy should be shaped.[1] In putting forward this suggestion it is not being overlooked that the Indian Legislature has no control over the loan policy of the Government of India. But as it has already been suggested

[1] Since the above was written the Government of India have announced their intention of adopting a policy for the redemption of debt which is based on the principles laid down by the Finance Member in his Budget speech of 1924–25. The Government of India having examined the whole position very carefully are of opinion that for the redemption of debt a sum of 4 crores from the revenues would be sufficient. To that amount would be added each year in respect of any new capital borrowing one-eightieth of the face value of the amount borrowed.

there is no constitutional difficulty which debars the Indian Legislature from having a say in the matter, it is its clear duty to remove the present cause of confusion.

The Provincial Governments have under the Reforms their own debt accounts. Their debts are made up of substantial sums transferred to their account as a part of the new financial arrangements, the amounts advanced to them since the inauguration of the Reforms, and the amounts raised by them in exercise of their own borrowing powers. The sums transferred to their account by the Central Government represented the irrigation capital outlay incurred by it to the end of the 1920–21, and the unredeemed portion of the Provincial Loan Account. It is not necessary to explain why the responsibility for the former charge should rest with the Provincial Government. Irrigation being now a provincial subject, it is in keeping with the new financial scheme that the capital expenditure incurred on irrigation before the introduction of the Reforms should be borne on the provincial accounts. The Provincial Governments have to pay interest[1] to the Central Government on the amounts so transferred, and though the repayment of these amounts is neither necessary nor contemplated, the Provincial Governments can repay these amounts either from their surplus revenue, or from the borrowed funds if they can reduce the interest charged thereby.[1] The Provincial Loan Account represents the account of the loans and advances made by each Provincial Government to the agriculturists in times of distress, or for the improvement of land to the co-operative societies, local bodies, and for a number of other miscellaneous purposes. Before the Reforms the Provincial Governments received money from the Government of India for financing these transactions, which had to be

[1] The advances carry interest at the following rate:

(a) In the case of the outlay up to 1916–17 at the rate of 3·3252 per cent.

(b) In the case of the outlay incurred after the year 1916–17 at the average rate of interest paid by the Governor-General on the loans raised in the open market since the end of the year.

repaid, and interest was paid for the amount outstanding on this account. Now the Provincial Governments have to finance their own loan transactions, but the amounts owed by them to the Government of India on the 1st April, 1921, have been treated as an advance on which they have to pay interest and which have to be repaid in twelve years. It is open to any Provincial Government to repay in any year an amount in excess of the fixed instalments.[1] The Government of India has also advanced money to the Provincial Governments since 1921 for meeting their deficits and some other heavy charges. The terms as to the interest on and repayment of the principal have to be settled in each case and depend upon the rate at which the Central Government can borrow money, the purpose for which the loan is required and other relevant considerations. The provinces can also raise loans on the credit of their own revenues. The purposes for which the loans can be floated have been prescribed by the rules. They can be raised for projects of lasting public utility of a remunerative character. When the funds are borrowed for the non-productive work of manifest utility, arrangements have to be made for the repayment of the loans within a certain period. The repayment of the loans when they are raised for irrigation or some other productive work is not obligatory. They can also be raised for providing funds for the Provincial Loan Account, relief of distress in times of famine, and for the redemption or the consolidation of outstanding loans. The loans may be raised in India or in England. For the loans raised in India the sanction of the Government of India has to be obtained. For sterling loans the sanction of the Secretary of State in Council is necessary, which has to be obtained by an application sent through the Government of India. The Government of India or the Secretary of State in Council can specify the rate of interest or the form of the issue. All loans, whether raised in England or in India, have to be issued in the name

[1] The Governments of the Punjab, Bengal, Assam, and Burma have taken the whole of the respective portions of the loan account on the 1st April, 1921, and allowed them to be adjusted out of their balances.

of the Secretary of State for India. The prescription of the purpose for which the loans can be raised, and retention of control over the conditions of the loans have been considered necessary to check the tendency of the public authorities to diminish their present burdens and add to their present resources, and avoid an unrestricted and wasteful competition among the borrowing authorities in India. Even when the provinces raise loans on the security of their allocated resources, the Government of India is responsible, though indirectly, for their repayment; for it may be assumed that the possibility of the Government of India allowing any Provincial Government to go bankrupt cannot even be contemplated. In view of this tacit guarantee which always must exist, it is desirable that the Government of India should approve of the conditions under which the loans are to be raised. The scope of the approval of the Government of India is limited to the examination of the borrowing proposals of the Provincial Government from the financial standpoint.[1]

[1] In order to systematize the arrangements for administrating the advances made by the Central to the Provincial Governments a central fund has been established with effect from the 1st April, 1925, to be called the "Provincial Loan Fund," out of which all advances granted by Government of India to the Provincial Governments will in future be made. The scheme has been outlined by the Government of India in a resolution, the operative portion of which is given below.

"All outstanding capital liabilities of the Provincial Governments to the Government of India will be transferred to the fund at the time of its constitution, and this capital will be increased from time to time as required by further advances from the Government of India. The rate of interest charged to the Government of India on advances to the fund will be determined in the same manner in which the rate of interest charged by the Government of India on advances to the provinces is now determined, that is to say, on the basis of the cost of new borrowing to the Government of India from time to time. If at any time there is a surplus in the capital of the fund not required, or not likely to be required at an early date for the purpose of the new advances, the fund will be entitled to apply such surplus towards the reduction of the advances previously made to it by the Government of India under the conditions as may be determined by the Government of India according to the circumstances of the case.

The terms already arranged between the Government of India and the provinces in regard to any advances sanctioned prior to the constitution of this fund will not be modified or affected in any way. The fund will simply take the place of the Government of India as one of the parties to these contracts *vis-à-vis* to the province concerned. The amount and the purpose of every advance which may be made by the fund to the Provincial Government will be determined as at present by

The expenditure from loan funds being subject to the sanction of the Provincial Councils, the scrutiny of these

the Government of India in the Finance Department, and the Assembly will be asked to vote the necessary supply under the head 'Advances to the Provincial Loan Fund.' Receipts into and disbursements from the fund will be recorded in the public account in the distinct head, 'Provincial Loan Fund.'

Advances of less than 5,00,000 for any scheme or group of work will not normally be made from the fund as being excluded by the principle laid down in Rule 2(A) of the Local Government (Borrowing) Rules, which requires that the proposed expenditure shall be so large that it can not be met from the current revenue.

The rules governing the grouping of the individual works for the purpose of this paragraph shall be the same as the rules which govern the grouping of works in order to determine the authority which is competent to sanction the total expenditure. The limit of 5,00,000, however, will not apply to capital expenditure: (*a*) on capital works, (*b*) in a commercial department which is working at such a profit as to fulfil the test of productivity imposed by the Secretary of State, (*c*) in commercial department whose accounts are maintained on a commercial basis.

No advances will be made out of the fund to any Provincial Government which do not provide annually out of their ordinary revenues sums sufficient to redeem, within a period not exceeding eighty years from the date on which they were originally borrowed, and the loans or advances which they may from time to time obtain, or have obtained from any source other than the fund. This condition, however, will not apply to the pre-Reforms debt. The standard rate of interest charged by the fund on the new advances will be so calculated, after taking into account repayments due to the fund or already existing advances, as to maintain the solvency of the fund. The standard rate will be charged by the fund on all advances required for capital expenditure which can be classed as productive under the rules on the subject approved by the Secretary of State. For all other advances the rate will be a quarter per cent above the standard rate.

All new advances made from the fund, and also all outstanding advances at present other than the debt relating to irrigation works constructed before the Reforms, liability for which was transferred to the Provincial Governments under the Reforms Scheme, will be subject to eventual repayment. It will be for the Government of India in the Finance Department to determine whether in any particular case repayments shall be by equated instalments of principal and interest, or otherwise, and whether due instalments may be postponed, or other exceptional arrangements made without threatening the solvency of the fund

The Government of India in the Finance Department shall maintain a schedule specifying the terms of years appropriate to the repayment of the advances required for various purposes and will communicate to all provinces any additions to or modifications of that schedule at the time that they are made. In the event of its being necessary to write off any part of the advance as irrecoverable, the loss shall not fall on the fund but shall be made the occasion of a special demand grant to be submitted to the Assembly.

The Government of India retain full power to refuse or suspend advances to the fund in any way if the financial position of India makes it imperative that it should be done. The existing rights of the provinces to borrow otherwise than in the form of advances shall not be impaired."

proposals from the administrative standpoint would involve interference with the financial autonomy of the provinces. The need for keeping the demand for loans within limits set by the essential principles of sound finance has already been referred to. It is for the Provincial Governments and the Legislatures to conduct the borrowing operations in accordance with such principles, and resist the temptation of accelerating the rate of public expenditure even for beneficent purposes, when it is likely to react adversely on the financial resources of the succeeding generations.

The total provincial debt on the 31st March, 1924, was about 101 crores. Out of it 87·4 crores represents the loans and advances by the Central Government, and 13·6 crores the loans raised by the Provincial Governments in the open market. The same amount is made up of 71·1 crores of the productive and 21·9 crores of the unproductive debt. The productive debt is mainly due to the expenditure on irrigation works, though a part of it also represents the investment of funds in the development of forests and the construction of railways. Since then the debt owed by the Provincial Governments to the Central Government has increased and now stands at 98·81 crores, and a further provision of 12·5 crores has been made in the budget of 1924–25 for loans to the Provincial Governments. The loans raised of 13·5 crores have been floated by the Bombay and the United Provinces Governments. The Punjab Government has since raised a loan of 2·38 crores on its own account. The total debt transferred to their account by the Central Government on the 1st April, 1921, was about 81 crores. The provincial debt has thus increased by 32·8 crores in four years, which is a large amount. The financial difficulties, which they have had to face in common with the Central Government, account for a part of the increase, but in any case it would not have been safe to borrow more freely in view of the inelastic character of the provincial resources. An addition of 40 per cent to the provincial debt in four years is quite substantial. It would be an unsound policy to go much faster in this direction.

That it is desirable that the loan policy of the Governments of India should be under the control of the Indian Legislatures has already been emphasized. There is no reason why the borrowing operations of the Government should not be placed on a statutory basis. The practice of obtaining the sanction of the British Parliament for loans raised in England should be discontinued, and all loans, whether raised in or outside India, should be approved by the Legislatures here before they are floated. The Executive Government may be given discretion within certain limits, but the general conditions under which they are raised should receive the legislative sanction. The need of imposing this check on the discretion of the Government is suggested by another very important consideration as well. The political tendencies of international borrowing are well known. The experience of the last century has invariably shown that the granting of credits by the strong to the weak Governments is the first step towards the adoption of an aggressive foreign policy, and almost inevitably leads to conquest and occupation of the less well-organized countries. That the bondholder has been a power behind the throne in a number of acts of international brigandage is an established fact of recent history. To quote from Adams: "An interchange of capital and credit between peoples of varying grades of political development must endanger the autonomy of the weaker states."[1] The foundation of the Egyptian subjection was laid by the loans advanced by the Rothschilds to the Khedive, and though the position has since been partly retrieved, the heavy price which Egypt has had to pay for accepting the financial assistance of the foreign nations is a lesson which the weak nations cannot afford to forget. China and Persia have the same tale to tell, and the fact that both of these countries retain their political independence is not due to the fault of their creditors, whose Governments have been, it is well known, entertaining designs on their political independence. The bankers and

[1] *Vide* Adams' "Public Debts," p. 28.

the jingoes have always worked hand in hand, and their alliance has in most cases been fatal for the independence of the impecunious nations. To use Adams' words once more, and it is difficult to put the matter more mildly, the international loans endanger the political autonomy of the weak nations. India has no autonomy to lose, but she is striving to regain it. Among the obstacles which have to be reckoned with by our political workers in their efforts to raise the political status of India, the fact that 75 per cent of our public debt is in the hands of the aliens must be reckoned as one. The argument has wider application, but since the question of the public debts is under consideration, other aspects of the matter may be overlooked. The authors of the Joint Report have taken special pains to press the claims of European commercial community on Indian consideration. One of the results incidental to the main purpose with which money has been invested by them and their kinsmen at home is that there is a well-organized group of moneyed people who have a stake in the stability of the "British" character of the Indian administration, and one of the expectations which have been implicitly held out to them, and which we are now required to respect, is that the political evolution of India would be slow and steady, and not marked by any sudden mutations. That it is so has been repeatedly brought to the notice of the public by the representations which the European Associations in India have made on the question of the constitutional advance of the country. The obligations which have been or may be incurred must, of course, be respected. India's resources even now are inadequate for meeting her capital requirements. We will have to borrow abroad for our productive undertakings. But it is necessary that the Indian Legislatures should take a far-sighted view of the matter, and while borrowing when necessary, they should not prejudice the cause of the political progress of the country. This can be done if the flotations of the loans are made subject to the approval of the Indian Legislatures. During the war India had the opportunity of buying up her

sterling debt by the use of her surplus resources, but as the other considerations made that course undesirable, it is now necessary for the Legislatures to keep our commitments to the foreign nations within limits lest they should increase the difficulties in the way of our political advancement. Till very recently London was the only money market in which the countries with future possibilities could raise loans for their capital expenditure. India was not the only country which borrowed mainly in London. But now the war has shifted the centre of gravity, and New York bids fair to become as good a market for the flotation of loans as London itself. The supply of capital in London being limited, there is no reason why we should not look far afield and explore the possibility of being able to raise loans in markets other than the English market. The terms offered by the Secretary of State for the sterling loans are not always determined by strictly business considerations. The 7 per cent loan which was issued in 1921 and over-subscribed before anyone in India knew anything about it, ought to convince us of the necessity of making the issue of the loans a matter of which the Indian Legislatures should have full cognizance. Our policy should be to borrow as little as possible in the foreign countries, and borrow when necessary on the least onerous terms.

The control of the public debt in India is vested in the Controller of Currency, who delegates some of his functions to the Deputy Controller of Currency in areas which are under the jurisdiction of the latter. There is a central Public Debt Office in Calcutta managed by the Imperial Bank on behalf of the Government of India, and there are Public Debt Offices at Bombay and Madras, managed by the Local Head Offices of the Imperial Bank. The rupee debt held in England is administered by the London branch of the Imperial Bank. The sterling debt is managed by the Banks of England and Ireland. A substantial part of the work in connection with the administration of the public debt falls on the Treasury and Sub-treasury Officers who have to pay interest on due dates and discharge other

duties in connection with the Government securities. The Imperial Bank is paid at the rate of Rs.2000 per crore, and the Banks of England and Ireland at the rate of £300 and £360 per million of debt registered in their books. The Provincial Governments have got to make their own arrangements for the loans issued by them on their own account.

CHAPTER XIII

LOCAL FINANCE

IN the preceding chapters nothing has been said about the financial constitutions of the local bodies. It is not usual to include the finances of the local bodies in the books dealing with the financial machinery of the State. It is, however, desirable to know their financial position and their relation to the financial organization of the country as a whole. It is not possible to give a connected account of the financial constitution of the local bodies. The variety of their form, the different stages of the political development through which they are passing, the increasing importance of the local conditions and circumstances in determining their constitution as a result of the local self-government having been made a transferred subject under the Reforms and the peculiar features of the problems of local finance make it difficult to describe their financial constitution in general terms. The description in the following paragraphs is necessarily fragmentary and brief. It is not necessary to dwell on the importance of the local bodies. It is generally admitted that as they are the training-ground of democracy, it is essential to vitalize them for the healthy working of the whole political system. The problem of local finance has been, all the world over, difficult to tackle on account of the necessity of reconciling what appear to be mutually repulsive ends. On one hand it is necessary to secure what has been called the "national minimum" of efficiency in local administration. The institutions, apart from their educative value, are of more than local importance. Their activities, or at least some of them have national importance, and it is, on that

account, desirable to realize a certain standard of efficiency in their performance. But if that leads to undue centralization and circumscribes the sphere of their spontaneous activity, they become the agency of the central authority and cease to be the organs of local self-government.

In India the problem presents itself in a specially acute form. Here the traditions of excessive control, which have till now retarded the growth of the local bodies, have to be swept aside. But the fact that they have so far been kept in the leading strings accounts for the absence of the sense of responsibility and appreciation of their position as the integral portions of the national system, and is responsible for the limited outlook which most of the members of the local bodies betray in the discharge of their public duties. It is difficult to find a *via media* between the two extremes of excessive official control and complete absence of the higher supervision, both of which have had injurious effect on the development of the local institutions. A great deal, of course, hinges on finance. It is necessary to give them adequate resources and abandon the attempt of protecting them from the consequences of their own mistakes. This must be done, if they are to have a fair chance of success. But in matters of finance, for want of training, if nothing else, the local prejudices and the desire to win easy popularity may give us a regime of local anarchy, the unwholesome effects of which may not be confined to the spheres of local finance. It is not possible to study the problem in detail in the limited compass of this book. All that can be attempted is to explain their present financial position and the general principles which govern their relations with the central authority. For different reasons it is proposed to exclude two kinds of local bodies from the scope of the remarks in the following paragraphs. The Punchayats, which have come into existence recently, are still in their experimental stage. The local self-government cannot become a reality in India unless they acquire a firm footing in the system of our public administration. But as it is they are in an embryonic stage, and

have on that account to be left out of account in the brief description of the finances of the local bodies. The Port Improvement and Trusts have, for another reason, to be omitted. They are special organizations created for special purposes. The need of having separate authorities for the functions which they perform has been questioned in some quarters. But without dealing with that aspect of the matter, it may be stated that they are not like other local bodies, urban and rural, and it is difficult to make any statement, which may apply to them as well as to the municipal and district boards, which form the bulk of the local institutions. It is convenient, therefore, to confine the bearing of the following observations to the latter bodies and say nothing about the Punchayats and Port and Improvement Trusts.

One general observation, with which we may introduce the subject, is that the local bodies being subordinate members of the larger political units, cannot be exempted altogether from outside control. Within the sphere assigned to them they may be given sufficient liberty of action to develop local initiative and enterprise, but the spheres within which they have to function, have to be demarcated by the central authority. Their duties, powers, and resources are defined in every country by higher political authority to which they are subordinate, and it is necessary to protect the interests of the latter against the incursions of the local bodies. It is, of course, unthinkable to give them the power to levy any taxes and spend their proceeds in any way they like. Their sources of income and the objects on which they can be spent have to be specified and any transgressions on their part beyond the limits laid down for them to be strictly guarded against. The restraints on the exercise of their financial powers within the spheres assigned to them may be removed in order to let them learn the right methods by following the policy of trial and error, but they cannot be allowed to ignore the limitations which are inherent in the fact of their existence as distinct political entities. It is necessary to

emphasize this consideration as there has been of late a tendency to underrate its importance, and spend the local funds for unauthorized purposes. No government, howsoever democratic, can give the municipal and rural corporations unfettered discretion in managing their finances. That would, besides producing utter confusion in the finances of the local bodies, give rise to friction among the local bodies themselves, and between them and the central authority, and throw the whole financial machinery out of gear.

In India the local bodies are under the Provincial Governments. Their constitution, functions and resources are regulated according to the provisions of the statutes which have brought them into existence. For the Presidency Corporations of Calcutta, Bombay, and Madras there are separate Acts. For the other urban and the rural boards, each province has got its own Municipal and District Boards Acts, according to which they are constituted. The outside control over them is exercised by the Local Self-government Department of the Provincial Government, which delegates some powers to the district officers and the commissioners. The control of the Government of India over the local bodies is confined to prescribing the taxes which the latter can impose, and limiting their borrowing powers. During the recent years the laws have been passed in different provinces to widen the scope and the powers of the local bodies. As a result of these measures their constitutions have been made more liberal, and certain financial restrictions, which were felt to be irksome, have been removed. As this process is carried further, the local bodies will have conditions provided for them for their success, provided the members of the local bodies have enough public spirit and the resourcefulness to take advantage of their opportunities.

The financial year of the local bodies is the same as the financial year of the Government. It commences on the 1st April. The annual estimates are prepared by the Executive Officer or the Chairman of the Board, who

obtains the necessary information from the heads of the departments. The estimates are made ready about two months before the expiry of the current year, and are examined by the Finance Sub-committee, if the Board has got one, and then submitted to the Board. The Board has generally got final powers for passing the estimates. But in certain cases the previous sanction of the district officer or the commissioner is required for passing them. In such cases the estimates are forwarded to those officers who can insist on the insertion or omission of certain items, and they are finally passed on their return from those officers. But generally speaking the estimates are disposed of by the Boards and a copy of sanctioned estimates has to be sent to the Provincial Government through the District Officers for their information. The Provincial Government has to satisfy itself that the obligatory functions of the Board have been duly provided for in the estimates. The Board has full authority to revise the budget in the course of the year, make supplementary provisions, authorize re-appropriations of savings from one head to another, subject to the condition of not reducing their balances below the minimum laid down by the Provincial Government. In the cases in which the approval of the Government Officer is necessary for passing the budget estimates, all proposals for reappropriations and supplementary provisions also require the approval of the same authority. But it may be stated that the control of the Government Officers over the framing of the budget estimates is a vanishing factor in the finances of the local bodies. Most of them have been granted final powers in this respect, and it may be hoped that before long all of them will be free to draw up their estimates without any external interference. The objects for which the provisions can be made have been defined. Their functions have been divided into two parts—obligatory and optional. The obligatory functions have priority over the optional ones in the allocation of local funds, and all local boards have within the limits of their resources to provide for them.

The local bodies derive their income from certain prescribed sources and vary the rates of taxes and fees subject to certain maximum and minimum limits. But the reduction of rates in the case of the indebted boards requires the sanction of the Provincial Governments.

The receipts of the local bodies are composed of income from taxes and fees, from other sources of income like rents from markets, sale of night soil, etc., and the grants-in-aid given from the provincial revenues. The taxes which the local authorities can impose are given in the Scheduled Taxes Rules.[1] The permission to impose taxes has to be granted by the Provincial Governments, and only those taxes are made use of by the local authorities which are suited to local conditions and are adequate for the local needs. The Provincial Governments also lay down the limits within which they can vary the rates without their previous sanction. The most important sources of income in case of the urban boards are the taxes on houses and buildings, the octroi or its substitute, the terminal tax, and the main source of income for the rural boards is the land cess, which is collected by the Provincial Governments and its yield is placed at the disposal of the rural bodies. The income of the local authorities from sources other than taxation is about the one third of their total revenues. They are capable of expansion, and on account of the inelasticity of the local taxes it is desirable to make use of them to a larger extent. It is admitted by the students of finance that the local bodies can apportion the benefits which the individuals derive from the services rendered by them with less difficulty than the central authorities, and they should, on that account, give greater weight to this consideration in raising their revenues. We have to utilize what is called the municipal trading more extensively for increasing our local funds. The grants-in-aid are given by the Governments either for general or for specific purposes. They generally bear a certain proportion to the expenditure incurred by the local bodies. Sydney Webb has called the

[1] *Vide* Appendix II.

grants-in-aid as "the necessary hinges in the flap" by which the necessary amount of supervision and control can be enforced without offending the susceptibilities of local autonomy and without losing the real advantage of local initiative and freedom to experiment.[1] In India, where the official control over the local bodies has gone as far as it can go anywhere, the grants-in-aid have merely been doles—a means of supplementing the limited resources of the local bodies. Now that the local bodies are being freed from their former restrictions, the grants-in-aid in India can also become a means of reconciling the interests of local autonomy with the interests of the community as a whole. The problem of the relation of the local and provincial revenues is as difficult of solution as the problem of the fiscal relations of the Provincial and the Central Governments. The economic life, not being based on local economy, it is difficult to allocate to the local bodies the sources of revenue whose incidence may be confined to the localities concerned. It has already been stated that the local bodies ought to make the benefit accruing from the services rendered by them the measure of the contributions, which they get from their constituents to a much greater extent than the higher public authorities can do, or in other words their income should be derived more from fees than from taxes. This principle has still to be embodied in the fiscal arrangements of the local bodies in India, but when this is done, local taxation will still be necessary. The growing demands that are being made on the resources of the local authorities in conformity with the trend of events in every other country of the world makes the expansion of their resources a national necessity. It is not possible to discuss the principles of the allocation of resources between the Provincial and the Local Governments, or suggest the means by which the local revenue can be increased. But it is worth while to state that the separation of resources should not be interpreted to mean

[1] *Vide* Introduction, written by Sydney Webb, to "National and Local Finance," by W. Grice.

that only those resources should be allotted to the local bodies which can be administered by them. The method of assessment and collection of certain taxes by the central authorities, the yield of which is wholly or partly assigned to the localities, is a method of raising revenue which has been found workable in a number of countries. A portion of the yield of the so-called death duties is reserved for the local divisions in the United Kingdom. In some of the American commonwealths the corporation and other taxes are assessed and collected by the State Governments, but are returned in part to the local divisions. The principle of separation of resources in the sense of each government having absolutely distinct resources of its own is desirable, but a well-rounded fiscal system cannot be secured unless it is supplemented by other principles, which may make it possible for the larger political units to share the proceeds of some sources of revenue with the subordinate public authorities. The fiscal basis must conform to the economic facts, and as the changes that are being worked out in economic life of the community are removing local barriers and introducing a greater degree of economic unity among the different parts of the country, the local bodies, if left to themselves, are likely to impose taxes which affect other localities and the country as a whole. It is on that account necessary to check their discretion and give them freedom of action within narrow and well-defined limits. But the same reason, which makes this check imperative, makes it highly desirable to allow the local bodies to share the proceeds of certain taxes, which may on account of the working of the economic forces have to be assessed and collected by the central authorities. This system of the apportionment of revenues between the central, provincial, and local authorities is less simple than the assignment of the distinct sources of income to each one of them, but being in accord with the working of the economic forces is likely to lead to a more lasting settlement of some of our pressing fiscal problems. The limitations of space make it necessary to leave the subject here with the statement

that though the question of local revenues has not as yet attracted public attention, it will soon force itself upon the notice of the public, and demand a satisfactory solution. The public needs will increase more rapidly in the domain of the local than in that of the Central and the Provincial Governments, and as the local taxes cannot keep pace with the growth of local needs, the problem of local revenues will become increasingly embarrassing.

The ordinary procedure for the collection of taxes and the other municipal dues is that the person liable for payment gets a bill from the local authority, and has to make payment in its office. If the payment is not made within two weeks a warning is issued, and if the amount due even then remains unpaid, the legal action is taken against the defaulter. In certain cases the system of outdoor collection is adopted. The tolls, certain fees and the octroi dues are collected by the tax-collector and paid duly into the municipal office. The land cess, which is the main source of income of the rural boards, is collected by the Provincial Governments. All local funds, with the exception of some advances, have to be deposited in the treasuries or the branches of the Imperial Bank.

The expenditure is incurred according to the provisions of the budget estimates, as modified by the later orders of the local authorities. The employees of the local bodies are not allowed to exceed the estimates without obtaining their previous sanction. The claims for payment from the local revenues are presented to the chief Executive Officers who have to examine them and, if they find them admissible, pass them for payment. The payments, unless the amounts are very small, are made by cheques drawn on the balances in the Treasury or the Bank. The establishment and other charges of the local bodies are paid on bills drawn on the prescribed forms, which have to be signed by the Executive Officers, and the amounts drawn on cheques for disbursement.

The form of the accounts, which have to be maintained by the local bodies, and the heads of the account under

which the receipts and expenditure are classified are prescribed by the Provincial Governments. The Audit Department of the Government of India has now been relieved of the responsibility of auditing the local accounts. The results of audit showing the technical irregularities and also matters of general importance, which require the particular attention of the local authorities, is communicated to the chairman of local body. The report of the auditor is considered at a meeting of the board soon after its receipt which decides the action it proposes to take on the points raised by him. Copies of the resolutions, in which the decisions are embodied, are sent to the auditor and to the officer, who receive the annual report of the board. The objections which the auditor cannot withdraw are settled either by the recovery of the amounts in question or are submitted for the orders of the Provincial Governments. The supervision exercised by the latter in matters of accounts and audit is a necessary safeguard against the mismanagement of local finances, and the misuse of funds. It does not reduce the autonomy of the local authorities and ensures the observance of the essential principles of sound finance.

The local bodies can raise money by loans. The loans may be obtained from the Provincial Governments, who lend money from the Provincial Loan Account, or raised in the open market. The loans raised in the open market require the sanction of the Government of India. The loans of the local authorities have to be repaid in all cases. The period in which the repayment is to take place varies in different cases but never exceeds sixty years. Annual provision has to be made for the redemption of loans. The borrowing is allowed for meeting heavy outlays, which cannot be met out of the annual revenues. It is generally done for works of public utility of non-remunerative character, though some of the rural boards in Madras have raised loans for providing feeder railways. The check over the borrowing powers of the local bodies is essential, as the tendency to throw burdens on the succeeding generations

and mortgage the future has been the bane of local finance in all countries. The increase of local indebtedness may, in some cases, be a proof of enterprise and vitality of the local authorities. The indebtedness of the local bodies is likely to increase faster in future, if they undertake productive works to improve the amenities of life and enlarge the local revenues. But the need for the control of the Provincial Governments on the borrowing of the local authorities will not grow less on that account. The local debts in other countries have been responsible for a lot of corruption in their public life. The use of credit by the local bodies has encouraged extravagance, made the local ratepayers careless as to how the local funds are being spent, and in several cases the practices, which otherwise would not have been tolerated for any length of time, have been regarded with indifference on account of the funds for the local projects having been obtained by borrowing. The local authorities in India have given abundant proof of their unwillingness to increase local taxes, and if the control of the Provincial Governments is relaxed in the slightest degree, they are likely to have recourse to the convenient way of providing the requirements of city life without any regard for the principles of sound finance. The local debts in India have not grown in a way as to cause any concern. The debt of the municipalities has grown from 16·5 crores in 1912 to 20·6 crores in 1921, and the debt of the district boards has practically remained stationary at 9 crores. The local bodies can with advantage borrow funds for many works of public utility, and, if they adopt a more ambitious programme of borrowing they can, without straining their credit, raise the necessary funds. But that will not dispense with the necessity of the Provincial Government exercising a vigilant control over the use of the public credit by the local authorities.

The local finance in India has not received the amount of attention which it deserves. The moribund condition in which a number of the municipalities and the district boards find themselves is partly the result of the circum-

spection of their financial powers. Their enlargement, with the stimulus which a vigilant public opinion can give, should improve matters and enable the local authorities to carve out for themselves many fresh spheres of activity. It is time for each Provincial Government to have the position thoroughly examined, and lay down certain broad principles for the guidance of the local authorities and itself in matters relating to local finance. With the development of homogeneous economic conditions the defects of the local finance are likely to be the same all over the country, and a concerted attempt on the part of all the provinces to approach and solve the problem on the basis of certain well-considered principles will go a long way to place the finances of the local bodies on a sound footing. The re-adjustments will necessarily take time, but the acceptance of a goal and an organized effort to reach it will be very helpful.

CHAPTER XIV

CONCLUSION

The analysis of our financial system has now been concluded. It is not easy to gather up the leading principles which emerge from our study. The constitutional aspect of the system generally receives much greater attention than the administrative and is, from the political standpoint, more important. The whole system is in the melting-pot. A great deal is happening behind the scenes which is of considerable importance on account of its effect on the future development of the system. The growth of democratic institutions in India will, as was stated in the first chapter, make it necessary to introduce changes of principle and procedure. The plastic stress of the new forces is bound to be felt in all Government departments and have a wholesome effect on their financial activities. The preparation of estimates and their execution must, under new circumstances, be done with greater care than before and show the influence of public opinion as expressed in and outside the Legislatures. The financial experts are chary of public criticism as it is generally unenlightened and based upon an imperfect appreciation of the intricacy of the financial questions. But when it is realized that the demands of the public are an expression of something more vital, the need for finding out the means by which these underlying forces may be made effective will become the concern of the financial experts themselves, who, knowing the mechanism in its details, are in a better position to put it to new uses. It is for them to take a lead in the matter and show how the objects for which the uninformed critics of the Government are agitating, can be better achieved by

the ways which their knowledge and experience suggest as being suited for the purpose. But if they adopt a passive attitude in the matter, and engrossed in details of administration fail to take into account or provide for the new needs of body politic, they should not be surprised if the organized public opinion pays no heed to their negative objections and takes a course which may, from their point of view, be based on ignorance and prejudice. Things are moving fast and cannot wait till our financial pharisees understand the inwardness of new events. Either they must be up and doing and place their trained judgement and ability at the disposal of the progressive forces or they will sweep past them, leaving them to derive whatever satisfaction they can from the confusion caused by their onward movement. In spheres of finance, it is true that the unseen is much greater than the seen, and the capacity to see the former and discrimination are absolutely essential. But little blame attaches to those who, not having having had the opportunities of knowing the working of a complicated system, are impatient at the absence of harmony between it and the new order of things which they want to establish. It is those who have eyes and still will not see that readjustments are necessary, upon whom will rest the responsibility for any damage that the financial apparatus may suffer on account of the undiscriminating zeal of the leaders of the national movement. The authors of the Joint Report have spoken of the future of the Indian Civil Service with great enthusiasm and anticipated for them a life which will indeed be more difficult but not less worthy on that account. "It is," as they put it, "harder to convince than to direct, to prevail in consultation than to enforce an order," and they are confident that the members of the Service will be as successful in the act of persuasion as they have been in that of government.[1] This confidence may or may not be well-placed, but it may be stated that those members of the superior services who are in charge of our financial

[1] *Vide* the Montagu-Chelmsford Report, para. 327.

administration have to play their rôle under the new regime with a more consummate skill. Their work being of a highly technical character may not be understood or even appreciated by those who have or may come into power, but they not only will have to convince and prevail in consultation with the latter, but also advise them as to how the system, which they have been working till now, can be changed to satisfy the new demands that are being made upon it. It is hard to convince, but it is harder to guide the men in power who have risen to it after a great deal of struggle. They are naturally more anxious to assert their newly-acquired rights than listen to the counsels of wisdom, and it is for the officers in charge of the system to offer their advice without offending the susceptibilities of those for whom it is intended. It is not easy or agreeable to have superior knowledge and ability and use it for the benefit of those who do not know but are in a position to demand. This work of readjustment can only be accomplished with a spirit of goodwill and mutual understanding—a condition which everyone desires to have but very few know how to establish.

The leaders of the national movement have on their part to realize that the financial system is a delicate machine which cannot stand much rough handling. In a sense there is a very intimate connection between finance and politics. Finance being the vehicle of the Government, it is difficult to separate the two even in thought. But there is another sense in which the two have, as far as possible, to be kept apart. The Acworth Committee, while arguing against the mixing up of politics and railways, have said that if their warning is disregarded "railways would corrupt politics and politics would corrupt railways." The same thing can, to a certain extent, be said of finance and politics. If the exigencies of the party politics are in any way allowed to influence or affect the working of the financial system and lead to the neglect of the principles of legitimate public finance it will result in the introduction of serious and insidious diseases in our public life, which it

will not be easy to remedy.) The United States of America has already been referred to as a country whose public life has become very rotten on account of the local and party considerations becoming a determining factor in the voting and spending of public money. In India there are latent tendencies which, if not kept in check by a sense of national duty, are likely to have a deteriorating effect on the future of our financial organization. It cannot be too often repeated that inasmuch as we are passing through a transitional stage of our national life, a wrong move now will not only have undesirable results in the immediate future but also create a bad precedent whose full effects will be felt by the coming generations. It is, therefore, the duty of our political leaders to be extremely careful in dealing with our finances, provide adequate safeguards against the misapplication of public funds, and have some patience with the restrictions which howsoever annoying they may be under the present circumstances, will, in the future, prevent the introduction of serious evils in our financial system. If a party victorious at the polls makes use of the financial powers, of which it is the trustee, for winning temporary triumphs in the Legislatures or gaining some party ends of passing importance, it will by its short-sighted action be creating a menace for the future and make the outlook still more gloomy than it is at present. The practical difficulties of securing constitutional advance, unsympathetic attitude of the financial experts and the complexity of our national problem make the temptation of ignoring this counsel of perfection and utilizing every available means for accelerating our political progress almost irresistible, but the path of least resistance is also the path of danger and an exercise of imagination and foresight will enable us to realize its evil consequences and avoid them. This primary requisite of acting wisely under very difficult circumstances is to be assiduous in gaining knowledge of the financial system as it is and understand the inter-relation of its various parts. It is easy to be bold when one does not know, but the courage which is the

result of knowledge and foresight is more valuable, because it enables us not only to demolish the institutions which have outlived their utility, but also build for the future.

The necessity of our financial experts and political leaders rising to the realities of the situation and doing nothing to prejudice its future development, is specially great in view of the fact that our present financial system has possibilities, which will make it an excellent system for the self-governing India. The fact that through the sequence of operations essential unity is observed in administering the finances of the Government and the distinct steps, into which the undertaking is divided, are so adjusted as to make up one harmonious whole, is of great significance for the future. From the preparation of estimates to the submission of the audit and appropriation reports, to the Legislatures and the Secretary of State, each process is treated as a link in an unbroken chain and planned and carried out with this end in view. The preparation of estimates of income and expenditure by the Executive, their presentation in a form which makes it possible for the fund-granting authority to review, criticize, approve or disapprove the issues raised and formulated by the Executive on basis of the consideration of the whole scheme of finance and its comparison with the results of the past years, the publicity which they are given by their discussion in the Legislatures and the limited control which the latter exercise in the determination of revenues and grant of funds, the expenditure of money according to appropriations and leaving to spending departments some discretion in respect of the detail of expenditure which enable them to depart from the assignment of funds under certain conditions and within certain limitations, the receipt, custody, and issue to the paying officers of the public funds and their movement from one part of the country to another to meet the public requirements, the concentration of balances and their maintenance at a particular level to ensure the solvency of the Government, the keeping and rendering of accounts with a

uniform nomenclature in order that at all times information may be available regarding the expenditure authorized or made and the state of public treasury, the audit of accounts by a trained and competent agency, and the preparation of reports in which the financial operations are duly reviewed and the results of audit set forth in a manner which enables the Government and the Legislature to have complete and detailed information regarding expenditure of funds granted by them—are operations which constitute the parts of one system, and dovetail into one another fairly well. The Indian system is characterized by unity and co-ordination—features which are well worth preserving in all the future developments which political progress or changed circumstances may make necessary.

The unity of the system is the result of administrative and financial centralization. Centralization is now a discredited word and as a phase of our political evolution it has no future. But even when it has been completely displaced by an arrangement which will afford scope for diversity of expression in all spheres of political life, the need of proper supervision and control in all stages of the administration of finance will remain, if the maximum of economy and efficiency is to obtain in the management of the system. For that it will be essential to retain the central executive control over its working. The supervision should begin at the starting point in the chain of operation—viz. the preparation of estimate, which, as it has been sufficiently emphasized, should embody some well-conceived policy and programme, and extend to all subsequent stages of financial administration. The control should be real and exercised by an agency independent of and superior to other departments of the Government. The chief merit of the English system, on which our system has been modelled, is due to the exceptional thoroughness with which the problem of control has been worked in actual operations of the Government. Our Finance Departments, both central and provincial, are, from the point of view of providing for the effective supervision and control, of

great potential importance. From the description of their functions and constitution which has already been given, it will appear that they are expected to be the organs of financial administration on which is to devolve the responsibility for preventing the mismanagement of finances. The opportunities for the misapplication of funds and waste exist almost at every step of the financial administration. In the estimating or appropriating for future needs, expenditure may be included for objects and purposes which are unimportant or relatively less important than others for which no or inadequate provision is made. In the collection of revenues all the dues accruing in the course of the year may not be realized, or even when realized may not be brought to account. In the expenditure of money the obligations may be incurred carelessly and inefficiently, excessive salaries may be paid, or materials may be purchased which are not required, or even when required their quality may be much higher than is needed for the proper discharge of public duties, and they may be paid for at rates for which there is no justification. The sums charged to the public treasury may be utilized for private ends, and in the custody of treasure loss may arise on account of carelessness or fraud. But what is perhaps the most potent cause—and one that is exceedingly difficult to avoid—of the waste of public money is the limited outlook of the different units of the Government, that are often likely to find their individual interests out of harmony with the interests of the Government as a whole. The officials in charge of the various branches of public service generally exaggerate the importance of their work and seek to secure for it the largest appropriation of funds that is possible to obtain. A feeling that effect of any moderation in their demands will be more than neutralized by the provision of extra funds for other services and open for them larger opportunities for extravagance strengthens the natural tendency of the subordinate branches of administration to get as much as they can and ask for more. On account of all these occasions of unnecessary or exces-

sive expenditure or waste of public money in other ways the need for consistent and thorough control over all the financial operations of the Government is too obvious to require further emphasis. It is for the Finance Departments to exercise vigilant supervision over them and prevent in every possible manner the misuse of funds. It is, therefore, necessary that the Finance Departments should be in position to discharge their functions in an efficient manner and get the support of the Legislature and the public in the performance of their duties. But the fact that the Finance Departments in India are under the direct control of the Secretary of State, and carry out his orders, has already antagonized the public against them and made them the object of bitter criticism both in and out of the Legislatures. It is difficult to suggest the means by which the situation can be improved without radical changes in the present constitution. It is not possible to pursue the point further. All that can be said is that efficiency and economy cannot be realized in the working of the system without the existence of effective treasury control. The understanding of its need and importance may be of some use in removing the prejudice against it.

The features of the system which have been commended above do not make it perfect even as a mechanism. Its defects are too glaring to be overlooked. They have already been mentioned. The existence of far-reaching control of the Secretary of State over the finances of the country is perhaps the most outstanding defect of the system. It militates against its unity and accounts for the inclusion of a number of items in the estimates, which are inserted therein without any reference to the financial situation as a whole. The other defects like the insufficiency of legislative control over the grant of funds, the determination of the sources of revenue and raising of funds by loans, lack of opportunities for the proper examination and discussion of estimates by the Legislature, absence of chief revenue authority in the provinces and general inefficiency of the revenue collecting departments, non-

existence of audit of receipts and stores, and lack of independence of the audit as a whole, combination of audit and account duties, preponderance of the external debts and several other shortcomings which have been referred to in detail in the preceding chapters are either due to the limitations of the present constitution which can only be removed by its revision or administrative imperfections which can and ought to be removed in the interest of its efficiency. It is admitted that the details of financial organization under the Reforms have not been worked out with as much care as they deserved. In the assignment of the sources of revenue to the Central and Provincial Governments the haste with which the distribution was effected has already brought its nemesis, and the early revision of the Meston Settlement is asked for by all who have given any thought to the question. The machine, in spite of its merits, is not working as smoothly as it can, and the need for the application of the lubricants and the removal of the gravel that has found its way into its different parts is manifest and cannot be put off much longer.

The defects in the financial structure may be removed, but from what has been said in connection with the different problems of administration, it must have become clear that the smooth working of the system does not merely depend upon its mechanical perfection. The most important factor, it need not be added, is the informing spirit which gives significance to the isolated facts and expresses a vital principle through them. The problem has its mechanics but cannot be solved without the understanding of its intimate connection with the rest of national life. In spite of the fact that our system is, in many respects, excellent, it is criticized oftener than it is approved, as the general belief is that it is not being worked in the best interests of the nation. The words like mechanism, apparatus, technique have been frequently used for the convenience of expression, but it is necessary to stress the fact that, if taken too literally they are likely to be mis-

leading. The problem is essentially organic, and though it has not been possible to take all its aspects into account, its close connection with larger questions of the national life has never been lost sight of. If the necessity of a fundamental change in the basis of our political fabric has not been emphasized often enough, it is because its imperative character has been taken for granted. The problem has been analysed separately as it is important and complex enough to merit a close study, and its understanding is essential for the solution of the larger issues on which the destiny of the nation depends. It is in the hope of contributing, in some small measure, to the fuller comprehension of the entire national problem that this book has been written. It is hoped that it has not been written in vain.

APPENDIX I

EXTRACT FROM THE GOVERNMENT OF INDIA ACT

SECTIONS GOVERNING THE FINANCIAL ADMINISTRATION

The Revenues of India :—

Application of revenues.

(20) (1) . . . The revenues of India shall be received for and in the name of His Majesty, and shall, subject to the provisions of this Act, be applied for the purposes of the Government of India alone.

(2) There shall be charged on the revenues of India alone :—

(*a*) All the debts of the East India Company ; and

(*b*) all the sums of money, costs, charges, and expenses which, if the Government of India Act, 1858 (21 & 22 Vict., c. 106) had not been passed, would have been payable by the East India Company out of the revenues of India in respect of any treaties, covenants, contracts grants or liabilities existing at the commencement of that Act ; and

(*c*) all expenses, debts and liabilities lawfully contracted and incurred on account of the Government of India ; and

(*d*) all payments under this Act 1 (except so far as is otherwise provided under this Act).

(3) The expression "the revenues of India" in this Act shall include all the territorial and other revenues of or arising in British India, and, in particular,—

(i) all tributes and other payments in respect of any territories which would have been receivable by or in the name of East India Company if the Government of India Act, 1858 (21 & 22 Vict., c. 106), had not been passed ; and

(ii) all fines and penalties incurred by the sentence or order of any Court of Justice in British India and all forfeitures for crimes of any movable or immovable property in British India ; and

(iii) all movable or immovable property in British India escheating or lapsing for want of an heir or successor, and all property in British India devolving as bona fide vacantia for want of a rightful owner.

(4) All property vested in, or arising or accruing from property and rights, His Majesty under Government of India Act, 1858 (21 & 22 Vict., c. 106), or this Act, or to be received or disposed of by the Secretary of State in Council under this Act shall be applied in aid of the revenues of India.

Control of Secretary of State over expenditure of revenues.

Subject to the provisions of this Act, and rules made thereunder, the expenditure of the revenue of India, both in British India and elsewhere, shall be subject to the Control of the Secretary of State in Council, and no grant or appropriation of any part of those revenues, or of any other property coming into possession of the Secretary of State in Council by virtue of the Government of India Act, 1858 (21 & 22 Vict., c. 106), or this Act, shall be made without the concurrence of a Majority of votes at meeting of the Council of India :

2. Provided that a grant or appropriation made in accordance with provisions or restrictions prescribed by the Secretary of State in Council with the concurrence of the Majority of votes at a meeting of the Council shall be deemed to be made with the concurrence of the majority of such votes.

Application of revenues to military operations beyond the frontier.

Except for preventing or repelling actual invasion of His Majesty's Indian Possessions, or under other sudden or urgent necessity, the revenues of India shall not, without the consent of both Houses of Parliament, be applicable to defraying the expenses of any military operations carried on beyond the external frontiers of those possessions by His Majesty's forces charged upon those revenues.

(1) Such parts of the revenues of India as are remitted to the United Kingdom, and all money arising or accruing in the United Kingdom from any property or rights vested in His Majesty for the purpose of the Government of India, or from the sale or disposal thereof, shall be paid to the Secretary of State in Council, to be applied for the purposes of this Act.

(2) All such revenues and money shall, except as by this section is provided, be paid into the Bank of England to the credit of an account entitled "The account of the Secretary of State in Council of India."

(3) The money placed to the credit of that account shall be paid out on drafts or orders, either signed by two members of the Council of India and countersigned by the Secretary of

State or one of his under secretaries or his assistant under secretary, or signed by the Accountant-General on the establishment of the Secretary of State in Council or by one of the two senior clerks in the Department of that Accountant-General and countersigned in such manner as the Secretary of State in Council directs; and any draft or order so signed and countersigned shall effectually discharge the Bank of England for all money paid thereon.

(4) The Secretary of State in Council may, for the payment of current demands, keep at the Bank of England such accounts as he deems expedient; and every such account shall be kept in such name and be drawn upon by such person, and in such manner, as the Secretary of State in Council directs.

(5) There shall be raised in the books of the Bank of England such accounts as may be necessary in respect of stock vested in the Secretary of State in Council; and every such account shall be entitled "The Stock Account of Secretary of State in Council of India."

(6) Every account referred to in this section shall be a public account.

Accounts to be annually laid before Parliament.

26 . . . (1) The Secretary of State in Council shall, within the first twenty-eight days during which Parliament is Sitting next after the first day of May in every year, lay before both Houses of Parliament—

(*a*) an account, for the financial year preceding that last completed, of the annual produce of the revenues of India, distinguishing the same under the respective heads thereof, in each of the several Provinces; and of all the annual receipts and disbursements at home and abroad for the purposes of the Government of India distinguishing the same under the respective heads thereof;

(*b*) . . . the latest estimates of the same for the financial year last completed;

(*c*) accounts of all stocks, loans, debts and liabilities chargeable on the revenues of India at home and abroad at the commencement and close of the financial year preceding that last completed, the loans debts and liabilities raised or incurred within that year, the amounts paid off or

discharged during that year, the rates of interest borne by those loans, debts and liabilities respectively, and the annual amount of that interest ;

1 (*d*) * * * * * * * *

(*e*) a list of the establishment of the Secretary of State in Council, and the salaries and the allowances payable in respect thereof.

(2) If any new or increased salary or pension of fifty pounds a year or upward has been granted or created within any year in respect of the said establishment, the particulars thereof shall be specially stated and explained at the foot of the account for that year.

(3) The account shall be accompanied by a statement, prepared from detailed reports from each province, in such form as best exhibits the moral and material progress and condition of India.

Audit of Indian accounts of United Kingdom.

27 . . . (1) His Majesty may, by warrant under his royal sign Manual, Countersigned by the Chancellor of the Exchequer, appoint a fit person to be auditor of the accounts of the Secretary of State in Council, and authorize that auditor to appoint and remove such assistants as may be specified in the warrant.

(2) The auditor shall examine and audit the accounts of the receipt, expenditure and disposal in the United Kingdom of all money, stores and property applicable for the purposes of this Act.

(3) The Secretary of State in Council shall, by the officers and servants of his establishment, produce and lay before the auditor all such accounts, accompanied by proper vouchers for their support, and submit to his inspection all books, papers and writings having relation thereto.

(4) The auditor may examine all such officers and servants of that establishment, being in the United Kingdom, as he thinks fit, in relation to such accounts and the receipt expenditure or disposal of such money, stores and property, and may for that purpose, by writing signed by him, summon before him any officer or servant.

(5) The officer shall report to the Secretary of State in Council

his approval or disapproval of the accounts aforesaid with such remarks and observations and relation thereto, as he thinks fit, specially noting cases if any, in which it appears to him that any money arising out of the revenues of India has been appropriated to purposes other than those to which they are applicable.

(6) The auditor shall specify in detail in his reports all sums of money, stores and property which aught to be accounted for, and are not brought into account, and have not been appropriated in conformity with the provisions of the law, or which have been expended or disposed of without due authority and shall also specify any defects, inaccuracies or irregularities which may appear in the accounts, or in the authorities, vouchers or documents having relation thereto.

(7) The auditor shall lay all his reports before both Houses of Parliament, with the accounts of the year to which the reports relate.

(8) The auditor shall hold office during good behaviour.

(9) There shall be paid to the auditor and his assistants out of the revenues of India, or out of moneys provided by Parliament, such salaries as His Majesty, by warrant signed and countersigned as aforesaid, may direct.

Classification of central and provincial subjects.

45 A. (1) Provision may be made by rules under this Act—

(*a*) for the classification of subjects, in relation to the functions of Government, as central and provincial subjects for the purpose of distinguishing the functions of the Governor-General in Council and the Indian Legislature;

(*b*) for the devolution of authority in respect of provincial subjects to Local Governments, and for the allocation of revenues or other moneys to those Governments;

(*c*) for the use under the authority of the Governor-General in Council of the agency of local governments in relation to central subjects, in so far as such agency may be found convenient, and for determining the financial conditions of such agency; and

(*d*) for the transfer from among the provincial subjects of subjects (in this Act referred to as "transferred sub-

jects ") to the administration of the governor acting with ministers appointed under this Act, and for the allocation of revenues or moneys for the purpose of such administration.

(2) Without prejudice to the generality of the foregoing powers, rules made for the above-mentioned purposes may—

(i) regulate the extent and conditions of such devolution allocation and transfer ;

(ii) provide for fixing the contributions payable by local governments to the Governor-General in Council, and making such contributions a first charge on the allocated revenues or moneys ;

(iii) provide for constituting a finance department in any province, and regulating the functions of that department ;

(iv) provide for regulating the exercise of the authority vested in the local government of a province over members of the public services therein ;

(v) provide for the settlement of doubts arising as to whether any matter does or does not relate to a provincial subject or a transferred subject, and for the treatment of matters which affect both a transferred subject and a subject which is not transferred ; and

(vi) make such consequential and supplemental provisions as appear necessary or expedient :

Provided that without prejudice to any general power of revoking or altering rules under this Act, the rules shall not authorize the revocation or suspension of the transfer of any subject except with the sanction of Secretary of State in Council.

(3) The powers of superintendence, direction, and control over local governments vested in the Governor-General in Council under this Act shall, in relation to transferred subjects be exercised only for such purposes as may be specified in rules made under this Act, but the Governor-General in Council shall be the sole judge as to whether the purpose of the exercise of such powers in any particular case comes within the purposes so specified.

(4) The expressions " central subjects " and " provincial subjects " as used in this Act mean subjects so classified under the rules.

Provincial subjects, other than transferred subjects are in this Act referred to as "reserved subjects."

Indian Budget. 1 | 67 A. (1) The estimated annual expenditure and revenue of the Governor-General in Council shall be laid in the form of a statement before both chambers of the Indian Legislature in each year.

(2) No proposal for the appropriation of any revenue or moneys for any purpose shall be made except on the recommendation of the Governor-General.

(3) The proposals of the Governor-General in Council for the appropriation of revenue or moneys relating to the following heads of expenditure shall not be submitted to the vote of the Legislative Assembly, nor shall they be open to discussion by either Chamber at the time when the annual statement is under consideration, unless the Governor-General otherwise directs—

(i) interest and sinking funds charges on loans; and
(ii) expenditure for which the amount is prescribed by or under any law; and
(iii) salaries and pensions of persons appointed by or with the approval of His Majesty or by the Secretary of State in Council; and
(iv) salaries of Chief Commissioners and Judicial Commissioners; and
(v) expenditure classified by the order of the Governor-General in Council as—
  (*a*) ecclesiastical;
  (*b*) political;
  (*c*) defence.

(4) If any question arises whether any proposed appropriation of revenue or moneys does or does not relate to the above heads the decision of the Governor-General on the question shall be final.

(5) The proposals of the Governor-General in Council for the appropriation of revenue and moneys relating to heads of expenditure not specified in the above heads shall be submitted to the votes of the Legislative Assembly in the form of demands for grants.

(6) The Legislative Assembly may assent or refuse its assent to any demand or may reduce the amount referred to in any demand by a reduction of the whole grant.

(7) The demands as voted by the Legislative Assembly shall be submitted to the Governor-General in Council, who shall, if he declares that he is satisfied that any demand which has been refused by the Legislative Assembly is essential to the discharge of his responsibilities, act as if it had been assented to notwithstanding the withholding of such assent or the reduction of the amount therein referred to, by the Legislative Assembly.

(8) Notwithstanding anything in this section the Governor-General shall have power, in cases of emergency, to authorize such expenditure as may, in his opinion, be necessary for the safety or tranquillity of British India or any part thereof.

Business and procedure in Governor's Legislative Councils.

72 D. (1) The provisions contained in this section shall have effect with respect to business procedure in Governor's Legislative Councils.

(2) The estimated annual expenditure and revenue of the province shall be laid in the form of a statement before the Council in each year, and the proposals of the Government for the appropriation of provincial revenues and other moneys in any year shall be submitted to the vote of the Council in the form of demands for grants. The Council may assent, or refuse its assent, to a demand, or may reduce the amount therein referred to either by a reduction of the whole grant or by the omission or reduction of any of the items of expenditure of which the grant is composed:

Provided that—

(a) Local Government shall have power, in relation to any such demand, to act as if it had been assented to, notwithstanding to withholding of such assent or the reduction of the amount therein referred to, if the demand relates to a reserved subject, and the Governor certifies that the expenditure provided for by the demand is essential to the discharge of his responsibility for the subject; and

(b) the Governor shall have power in cases of emergency to authorize such expenditure as may be in his opinion necessary for the safety or tranquillity of the province or for the carrying on of any department; and

(c) no proposal for the appropriation of any such revenues or other moneys for any purpose shall be made except on

the recommendation of the Governor communicated to the Council.

(3) Nothing in the foregoing sub-section shall require proposals to be submitted to the Council relating to the following heads of expenditure :—

(i) Contributions payable by the Local Government to the Governor-General in Council ; and

(ii) interest and sinking fund charges on loans ; and

(iii) expenditure of which the amount is prescribed by or under any law ; and

(iv) salaries and pensions of persons appointed by or with the approval of His Majesty or by the Secretary of State in Council ; and

(v) salaries of Judges of the High Court of the province and of the Advocate-General.

(4) If any question arises whether any proposed appropriation of moneys does or does not relate to the above heads of expenditure, the decision of the Governor shall be final.

80-A (3) The local legislature of any province may not, without the previous sanction of the Governor-General, make or take into consideration any law—

(*a*) Imposing or authorizing the imposition of any new tax unless the tax is a tax scheduled as exempted from this provision by rules made under this Act ; or

(*b*) affecting the public debt of India, or the customs duties, or any other tax or duty for the time being in force and imposed by the authority of the Governor-General in Council for the general purposes of the Government of India, provided that the imposition or alteration of a tax scheduled as aforesaid shall not be deemed to affect any such tax or duty

Financial proposals.

80-C It shall not be lawful for any member of any local legislative Council to introduce, without the previous sanction of the Governor, Lieutenant-Governor or Chief Commissioner, any measure affecting the public revenues of a province, or imposing any charge on those revenues.

APPENDIX II

EXTRACT FROM THE DEVOLUTION RULES

Financial arrangements

Allocation of revenue.

14. (1) The following sources of revenue shall in the case of Governor's Provinces and in the Province of Burma, be allocated to the Local Government as sources of provincial revenue, namely :—

(*a*) Balances standing at the credit of the province at the time when the Act comes into force ;
(*b*) receipts accruing in respect of provincial subjects ;
(*c*) a share (to be determined in the manner provided by Rule 15) in the growth of revenue derived from income-tax collected in the province, so far as that growth is attributable to an increase in the amount of income assessed ;
(*d*) recoveries of loans and advances given by the Local Government and of interest paid on such loans ;
(*e*) payments made to the Local Government by the Governor-General in Council or by other Local Governments, either for services rendered or otherwise ;
(*f*) the proceeds of any taxes which may be lawfully imposed for provincial purposes ;
(*g*) the proceeds of any loans which may be lawfully raised for provincial purposes ; and
(*h*) any other sources which the Governor-General in Council may by order declare to be sources of provincial revenue.

(2) The revenues of Berar shall be allocated to the Local Government of the Central Provinces as a source of provincial revenue. This allocation shall be subject to the following conditions, namely :—

(i) That the Local Government of the Central Provinces shall be responsible for the due administration of Berar ; and

(ii) that if in the opinion of the Governor-General in Council provision has not been made for expenditure necessary for the safety and tranquillity of Berar, the allocation shall be terminated by order of the Governor-General in Council, or diminished by such amount as the Governor-General in Council may by order in writing direct.

15. (1) There shall be allocated to each Local Government a share in the income-tax collected under the India Income-tax Act, 1918, within its jurisdiction. The share so allocated shall be three pies on each rupee brought under assessment under the said Act in respect of which the income-tax assessed has been collected.

(2) In consideration of this allocation, each Local Government shall make to the Governor-General in Council a fixed annual assignment of a sum to be determined by the Governor-General in Council as the equivalent of the amount which would have accrued to the Local Government of the year 1920–21 (after deducting the provincial share of the cost of special income-tax establishment of that year) had the pie rate fixed under sub-rule (1) been applied in that year, due allowance being made for any abnormal delays in collection of the tax.

(3) The cost of special income-tax establishments employed within a province shall be borne by the Local Government and the Governor-General in Council in the proportions of 25 per cent and 75 per cent respectively.[1]

Payment of Government revenues into the public account.

16. All moneys derived from sources of provincial revenue shall be paid into the public account of which the Governor-General in Council is custodian, and credited to Government of the Province. The Governor-General in Council shall have power, with the previous sanction of the Secretary of State in Council, to prescribe by general or special order the procedure to be followed in the payment of moneys into, and in the withdrawal, transfer and disbursement of moneys from, the public account, and for the custody of moneys standing in the account.

Contribution by the Local Governments in 1921–22.

17. In the financial year 1921–22 contributions shall be paid to the Governor-General in Council by the Local Governments mentioned below according to the following scale :—

[1] This rule, as already stated on p. 161, has since been revised and simplified.

Name of province	Contributions (in lacs of rupees).
Madras	348
Bombay	56
Bengal	63
United Provinces	240
Punjab	175
Burma	64
Central Provinces and Berar	22
Assam	15

Contributions in subsequent years.

18. From the financial year 1922–23 onwards a total contribution of 983 lacs or such smaller sum as may be determined by the Governor-General in Council, shall be paid to the Governor-General in Council by the Local Governments mentioned in the preceding rule. When for any year the Governor-General in Council determines as the total amount of the contribution a smaller sum than that payable for the preceding year, a reduction shall be made in the contributions of those Local Governments only whose last previous annual contribution exceeds the proportion specified below of the smaller sum so determined as the total contribution; and any reduction so made shall be proportionate to such excess :—

Madras	17–90ths.
Bombay	13–90 ,,
Bengal	19–90 ,,
United Province	18–90 ,,
Punjab	9–90 ,,
Burma	6½–90 ,,
Central Provinces and Berar	5–90 ,,
Assam	2½–90 ,,

19. In cases of emergency the Local Government of any province may be required by the Governor-General in Council, with the sanction of, and subject to the conditions approved by, the Secretary of State, to pay the Governor-General in Council a contribution for any financial year in excess of the amount required by the preceding rules in the case of that year.

Priority of contributions.

20. The contributions and assignments fixed under the preceding rules shall be a first charge on the allocated revenues and moneys of the Local Governments concerned, and shall be paid in such instalments, in such manner, and on such dates as the Governor-General in Council may prescribe.

Withdrawal of balances.

21. At any time which he considers this course to be essential in the financial interests of India as a whole, the Governor-General in Council shall have power to require any Local Government to which revenues have been allocated under these rules so to regulate its programme of expenditure as not to reduce the balance at its credit in the public account on a specified date or dates below a stated figure, and shall have power to take the necessary steps by the restriction of issues of money to secure this end. Subject to this power, those Local Governments shall be at liberty to draw up their balances, provided that notice of the amount which they propose to draw during the ensuing financial year is given to the Governor-General in Council before such date in each year as the Governor-General in Council may by order fix.

Interest on Provincial balances.

22. Whenever the Governor-General in Council has, on receipt of due notice of the intention of the Local Government to draw on its balances, required it to reduce the extent of the proposed draft, he shall at the end of the financial year in which the Local Government is barred from drawing, credit the Local Government with interest on the amount which it was not permitted to draw. Such interest shall be calculated at the average rate at which the Governor-General in Council has borrowed money in the open market during the year by the issue of treasury bills.

Loan Account. Provincial

23. Any moneys which, on the first day of April, 1921, are owed to the Governor-General in Council on account of advances made from the provincial loan account of any province shall be treated as an advance to the Local Government from the revenues of India, and shall carry interest at a rate calculated on the average rate carried by the total amount owed to the Governor-General in Council on this account on the 31st March, 1921. The interest shall be payable upon such dates as the Governor-General in Council may fix. In addition, the Local Government shall pay the Governor-General in Council in each year as instalment in

repayment of the principal amount of the advance, and this instalment shall be so fixed that the total advance shall, except wherefore special reasons the Governor-General in Council may otherwise direct, be repaid before the expiry of twelve years. It shall be open to any Local Government to repay in any year an amount in excess of the fixed instalment.

Capital expenditure on irrigation works.

24. (1) The capital sums spent by the Governor-General in Council upon the construction in the various provinces of productive and protective irrigation works financed from loan funds, as may from time to time be handed over to the management of Local Governments, shall be treated as advances made to the Local Governments from the revenues of India. Such advances shall carry interest at the following rates, namely :—

(*a*) In case of outlay up to the end of the financial year 1916–17, at the rate of 3.3252 per centum ;

(*b*) In the case of outlay incurred after the financial year 1916–17, at the average rate of interest paid by the Governor-General in Council on loans raised in the open market since the end of that year.

(2) The interest shall be payable upon such dates as the Governor-General in Council may fix.

Advances by the Government of India.

25. The Governor-General in Council may at any time make to a Local Government an advance from the revenues or moneys accruing to the Governor-General in Council on such terms as to interest and repayment as he may think fit.

Priority of interest charges.

26. The payment of interest on loans and advances made under the three preceding rules and the repayment of the principal of an advance under Rule 23 shall be a charge on the annual allocated revenues of the Local Government, and shall have priority over all other charges, save only contributions payable to the Governor- General in Council.

Powers of sanctioning transferred expenditure.

27. The Local Government of a Governor's Province shall not, without the previous sanction of the Secretary of State in Council or of the Governor-General in Council, as the case may be, include any proposal for expenditure on a transferred subject in a demand for a grant, if such sanction is required by the provisions of Schedule III to these rules.

(2) Subject to the provisions of sub-rule (1), the Local Government of a Governor's Province shall have power to sanction expenditure on transferred subjects to the extent any grant voted by the Legislative Council.

(3) The Local Government of a Governor's Province shall have power to sanction any expenditure on transferred subjects which relates to the heads enumerated in section 72 D (3) of the Act, subject to the approval of the Secretary of State in Council, or of the Governor-General in Council if any such approval is required by any rule for the time being in force.

Delegation of powers of sanction.

28. (1) The powers of a Local Government under the preceding rule to sanction expenditure may be delegated by the Local Government to an authority subordinate to it, after previous consultation with the Finance Department, to such extent as may be required for the convenient and efficient despatch of public business.

(2) Any sanction accorded under these rules shall remain valid for the specified period for which it is given, subject, in the case of voted expenditure, to the voting of grants in each year.

Famine Insurance Fund.

29. Each Local Government mentioned in Schedule IV shall establish and maintain out of provincial revenues a famine insurance fund in accordance with the provisions of that Schedule, and such fund shall be controlled and administered as required by those provisions.

Taxation and borrowing.

30. All proposals for raising taxation or for the borrowing of money on the revenues of the province shall, in the case of a Governor's Province, be considered by the Governor with his Executive Council and Ministers sitting together, but the decision shall thereafter be arrived at by the Governor in Council or by the Governor and Minister or Ministers, according as the proposal originates with the Governor in Council or the Governor and Ministers.

Allocation of revenues for the administration of transferred subjects.

31. Expenditure for the purpose of the administration of both reserved and transferred subjects shall, in the first instance, be a charge on the general revenues and balances of each province, and the framing of proposals for expenditure in regard to transferred and reserved subjects will be a matter for agreement between that part of the Government which is responsible for the administration of the transferred subjects

and that part of the Government which is responsible for the administration of the reserved subjects.

Procedure in event of failure to agree.

32. (1) If at the time of the preparation of the budget the Governor is satisfied that there is no hope of agreement within a reasonable time between the Members of his Executive Council on the one hand and the Ministers on the other as to the apportionment of funds between reserved and transferred departments, respectively, he may, by order in writing, allocate the revenues and balances of the province between reserved and transferred subjects, by specifying the fractional proportions of the revenues and balances which shall be assigned to each class of subject.

(2) An order of allocation under this rule may be made by the Governor either in accordance with his own discretion, or in accordance with the report of an authority to be appointed by the Governor-General in this behalf on the application of the Governor.

Period of order of allocation.

33. Every such order shall (unless it is sooner revoked) remain in force for a period to be specified on the order, which shall be not less than the duration of the then existing Legislative Council, and shall not exceed by more than one year the duration thereof :

Provided that the Governor may at any time, if his Executive Council and Ministers so desire, revoke an order of allocation or make such other allocation as has been agreed upon by them :

Provided further, that if the order which it is proposed to revoke was passed in accordance with the report of an authority appointed by the Governor-General, the Governor shall obtain the consent of the Governor-General before revoking the same.

Condition of order of allocation.

34. Every order of allocation made under these rules shall provide that if any increase of revenue accrues during the period of the order on account of the imposition of fresh taxation, that increase, unless the legislature otherwise directs, shall be allocated in the aid of that part of the Government by which the taxation is initiated.

Preparation of budget in default of agreement or order of allocation.

35. If at the time of the preparation of any budget no agreement or allocation such as is contemplated by these rules has been arrived at, the budget shall be prepared on the basis of the aggregate grants respectively provided for the reserved and transferred subjects in the budget of the year about to expire.

Finance Department.

36. (1) There shall be in each Governor's Province a Finance Department which shall be controlled by a member of the Executive Council.

(2) Immediately subordinate to the member there shall be a Financial Secretary, with whom shall be associated, if the Ministers so desire, a Joint Secretary appointed by the Governor after consultation with the Ministers.

(3) The Joint Secretary shall be specially charged with the duty of examining and dealing with financial questions arising in relation to transferred subjects and with proposals for taxation or borrowing put forward by any Minister.

Functions of Finance Department.

37. The Finance Department shall perform the following functions, namely :—

(*a*) It shall be in charge of the account relating to loans granted by the Local Government, and shall advise on the financial aspect of all transactions relating to such loans ;

(*b*) it shall be responsible for the safety and proper employment of the famine insurance fund ;

(*c*) it shall examine and report on all proposals for the increase or reduction of taxation ;

(*d*) it shall examine and report on all proposals for borrowing by the Local Government ; shall take all steps necessary for the purpose of raising such loans as have been duly authorized ; and shall be in charge of all matters relating to the service of loans ;

(*e*) it shall be responsible for seeing that proper financial rules are framed for the guidance of other departments and that suitable accounts are maintained by other departments and establishments subordinate to them ;

(*f*) it shall prepare an estimate of the total receipts and disbursements of the province in each year, and shall be responsible during the year for watching the state of the Local Government's balances ;

(*g*) in connection with the budget and with supplementary estimates—

(i) it shall prepare the statement of estimated revenue and expenditure which is laid before the Legislative Council in each year and any supplementary esti-

mates or demands for excess grants which may be submitted to the vote of the Council ;

(ii) for the purpose of such preparation, it shall obtain from the departments concerned material on which to base its estimates, and it shall be responsible for the correctness of the estimates framed on the material so supplied ;

(iii) it shall examine and advise on all schemes of new expenditure for which it is proposed to make provision in the estimates and shall decline to provide in the estimates for any scheme which has not been so examined ;

(*h*) on receipt of a report from an audit officer to the effect that expenditure for which there is no sufficient sanction is being incurred, it shall require steps to be taken to obtain sanction or that the expenditure shall immediately cease ;

(*i*) it shall lay the audit and appropriation reports before the committee on Public Accounts, and shall bring to the notice all expenditure which has not been duly authorized and any financial irregularities ;

(*j*) it shall advise departments responsible for the collection of revenue regarding the progress of collection and the methods of collection employed.

Powers of Finance Department with reference to the reappropriation.

38. (1) After grants have been voted by the Legislative Council—

(*a*) the Finance Department shall have power to sanction any reappropriation within a grant from one major, minor or subordinate head to another ;

(*b*) the Member or Minister in charge of a department shall have power to sanction any reappropriation within a grant between heads subordinate to a minor head which does not involve undertaking a recurring liability, provided that a copy of any order sanctioning such a reappropriation shall be communicated to the Finance department as soon as it is passed.

(2) The Finance Department shall have power to sanction the delegation by a Member or Minister to any officer or class of

officers of the power of reappropriation conferred on such Member or Minister by clause (1) (*b*) above.

(3) Copies of orders sanctioning any reappropriation which does not require the sanction of the Finance Department shall be communicated to that department as soon as such orders are passed.

Matters to be referred to Finance Department.

39. No expenditure on any of the heads detailed in section 72 D (3) of the Act, which is in excess of the estimates for that head shown in the budget of the year, shall be incurred without previous consultation with the Finance Department.

Establishment charges.

40. No office may be added to, or withdrawn from the public service in the province and the emoluments of no post may be varied except after consultation of the Finance Department; and when it is proposed to add a permanent or temporary post to the public service, the Finance Department shall, if it thinks necessary, refer for the decision of the Audit Department the question whether the sanction of the Secretary of State in Council is, or is not, necessary.

Allowances and pay.

41. No allowance and no special or personal pay shall be sanctioned for any post or class of posts, or for any Government servant without previous consultation with Finance Department.

Grants and concessions.

42. No grant of land or assignment of land revenue, except when the grant is made under the ordinary revenue rules of the province, shall be given without previous consultation with the Finance Department; and no concession, grant or lease of mineral or forest rights, or right to water power or right-of-way or other easement, and no privilege in respect of such rights shall be given without such previous consultation.

Abandonment of revenue, etc.

43. No proposal involving an abandonment of revenue for which credit has been taken in the budget, or involving expenditure for which no provision has been made in the budget, shall be submitted for the consideration of the Local Government or the Legislative Council, nor shall any orders giving effect to such proposals issue without a previous reference to the Finance Department.

Disposal of reports by Finance Department.

44. Every report made by the Finance Department on any matter on which it is required to advise or report under these rules shall be forwarded to the department concerned and shall, if the Finance Department so require, be submitted by the department concerned to the Governor for the orders of the Local Government. The Governor may, if he thinks fit, direct that any such report shall be laid before the committee on public accounts.

Presumption of assent of Finance Department.

45. Wherever previous consultation with the Finance Department is required by these rules it shall be open to that department to prescribe, by general or special order, cases in which its assent may be presumed to have been given.

Agency

Agency employment of Local Governments.

46. The Governor-General in Council may employ the agency of the Governor in Council of any province in the administration of central subjects in so far as such agency may be found convenient.

Cost of agency establishments.

47. The cost of an establishment exclusively employed on the business of agency shall be a charge against all-India revenues.

Distribution of cost of joint establishment.

48. If a joint establishment is employed upon the administration of central and provincial subjects, the cost of such establishment may be distributed in such manner as the Governor-General in Council and the Governor in Council of the province concerned may agree, or, in the case of disagreement, in such manner as may be determined by the Secretary of State in Council.

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SCHEDULE III

RULES RELATING TO TRANSFERRED SUBJECTS

(1) 1. The previous sanction of the Secretary of State in Council is necessary :

(1) to the creation of any new or the abolition of any existing permanent post, or to the increase or reduction of the pay attached to any permanent post, if the post in either case is one which would ordinarily be held by a

member of an all-India service, or to the increase or reduction of the cadre of an all-India service ;

(2) to the creation of a permanent post on a maximum rate of pay exceeding Rs.1200 a month ; or the increase of the maximum pay of sanctioned permanent post to an amount exceeding Rs.1200 a month ;

(3) to the creation of a temporary post with pay exceeding Rs.4000 a month, or to the extension beyond a period of two years of a temporary post with pay exceeding Rs.1200 a month ;

(4) to the grant to any officer of an allowance, pension or gratuity which is not admissible under rules made, or for the time being in force under Section 96 B of the Act ; and

(5) to any expenditure on the purchase of imported stores or stationery otherwise than in accordance with such rules as may be made in this behalf by the Secretary of State in Council.

2. (1) Every application for the sanction of the Secretary of State in Council required by paragraph 1 shall be addressed to the Governor-General in Council, who shall, save as hereinafter provided, forward the same with his recommendation and with such further explanations of the proposal as he may have seen fit to require from the Local Government, to the Secretary of State in Council.

(2) If the application relates to :

(*a*) the grant in an individual case of any increase of pay, or

(*b*) the creation of a temporary post, the Governor-General in Council may, at his discretion, on behalf of the Secretary of State in Council, sanction the proposal, shall forward the application with his recommendation, and with such further explanations of the proposal as he may have seen fit to require from the Local Government, for the orders of the Secretary of State in Council.

SCHEDULE IV

1. The Local Governments mentioned below shall, save as hereinafter provided, make in every year provision in their budgets for expenditure upon relief, and insurance against

famine of such amounts respectively (hereinafter referred to as the annual assignments) as are stated against each :—

	Rs.
Madras	6,61,000
Bombay	63,69,000
Bengal	2,00,000
United Province . . .	39,60,000
Punjab	3,81,000
Burma	67,000
Bihar and Orissa . . .	11,62,000
Central Province . . .	47,26,000
Assam	10,000

(2) The provision shall be made in the shape of a demand for a grant, and the estimates shall show, under the major heads concerned, the method in which it is proposed to utilize the grant.

3. The grant shall not be expended save upon the relief of famine or upon the construction of protective irrigation works or other works for the prevention of famine. Any portion of the grant which is not so spent shall be transferred to the famine insurance fund of the province.

4. The famine insurance fund shall consist of the unexpended balance of the annual assignments for each year, transferred to the fund under paragraph 3 of this Schedule, together with any interest which may accrue on these balances.

5. The Local Government may, in any year when the accumulated total of the famine insurance fund of the province is not less than six times the amount of the annual assignment, suspend temporarily the provision of the annual assignment.

6. The famine insurance fund shall form part of the general balances of the Governor-General in Council, who shall pay at the end of each year interest on the average of the balances held in the fund on the last day of each quarter. The interest shall be calculated at the average rate at which the Governor-General in Council has during the year borrowed money by the issue of treasury bills. Such interest shall be credited to the fund.

7. The Local Government may at any time expend the balances at its credit in the famine insurance fund for any of the purposes specified in paragraph 3 of this schedule.

8. Such balances may further be utilized in the grant of loans to cultivators, either under the Agriculturists' Loans Act, 1884, or for relief purposes. When such loans have been granted, payments of interest on loans and repayments of principal shall be credited to the fund as they occur, and irrecoverable loans written off shall form a final charge against the fund.

9. In case of doubt whether the purpose for which it is proposed to spend any portion of the annual assignment of the famine insurance fund is one of the purposes specified in paragraph 3 of this Schedule, the decision of the Governor shall be final.

10. The annual accounts of the annual assignments and of the fund shall be maintained in forms to be prescribed in this behalf by the Auditor-General.

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C.—*Local Government (Borrowing) Rules*

Short title and commencement.

1. (1) These rules may be called the Local Government (Borrowing) Rules.

(2) They shall come into force on a date to be appointed by the Governor-General in Council, with the approval of the Secretary of State in Council, and different dates may be appointed for different parts of India.

Purposes for which loans may be raised.

2. A Local Government may raise loans on the security of the revenues allocated to it for any of the following purposes, namely :—

(*a*) To meet capital expenditure on the construction or acquisition (including the acquisition of land, maintenance during construction and equipment) of any work or permanent asset of a material character in connection with a project of lasting public utility, provided that

(i) the proposed expenditure is so large that it cannot reasonably be met from current revenues ; and

(ii) if the project appears to the Governor-General in Council unlikely to yield a return of not less than such percentage as he may from time to time by order prescribe, arrangements are made for the amortization of the debt ;

(*b*) to meet any classes of expenditure on irrigation which have under rules in force before the passing of the Act been met from loan funds ;

(*c*) for the giving of relief and the establishment and maintenance of relief works in times of famine or scarcity ;

(*d*) for the financing of the Provincial Loan Account ; and

(*e*) for the repayment or consolidation of loans raised in accordance with these rules or the repayment of advances made by the Governor-General in Council.

Sanction to loans.

3. (1) No loan shall be raised by a Local Government without the sanction (in the case of loans to be raised in India) of the Governor-General in Council or (in the case of loans to be raised outside India) of the Secretary of State in Council, and in sanctioning the raising of a loan the Governor-General in Council or the Secretary of State in Council, as the case may be, may specify the amount of issue, and any or all of the conditions under which the loan shall be raised.

(2) Every application for the sanction of the Secretary of State required by this rule shall be transmitted through the Governor-General in Council.

Priority.

4. Every loan raised by a Local Government in accordance with these rules shall be a charge on the whole of the revenues allocated to the Local Government, and all payments in connection with the service of such loans shall be made in priority to all payments by the Local Government other than the payments of :—

(i) the fixed provincial contribution payable to the Governor-General in Council,

(ii) interest due on sums advanced to the Local Government by the Governor-General in Council from the revenues of India, and

(iii) interest due on all loans previously raised by the Local Government.

D.—Scheduled Taxes Rules

Short title and commencement.

1. (1) These rules may be called the Scheduled Taxes Rules.

(2) They shall come into force on a date to be appointed by the Governor-General in Council, with the approval

of the Secretary of State in Council, and different dates may be appointed for different parts of India.

Taxes which may be imposed for purposes of the Local Government.

2. The Legislative Council of a province may, without the previous sanction of the Governor-General, make and take into consideration any law, imposing, for the purposes of the Local Government, any tax included in schedule I to these rules.

Taxes which may be imposed for purposes of local authorities.

3. The Legislative Council of a province may, without the previous sanction of the Governor-General, make and take into consideration any law imposing, or authorizing any local authority to impose, for the purposes of such local authority, any tax included in Schedule II to these rules.

Additions to schedules.

4. The Governor-General in Council may at any time, by order, make any addition to the taxes enumerated in Schedules I and II to these rules.

Saving.

5. Nothing in these rules shall affect the right of a local authority to impose a tax without previous sanction or with the previous sanction of the Local Government when such right is conferred upon it by any law for the time being in force.

SCHEDULE I

1. A tax on land put to uses other than agricultural.
2. A tax on succession or on acquisition by survivorship in a joint family.
3. A tax on any form of betting or gambling permitted by law.
4. A tax on advertisements.
5. A tax on amusements.
6. A tax on any specified luxury.
7. A registration fee.
8. A stamp duty other than duties of which the amount is fixed by Indian legislation.

SCHEDULE II

1. A toll.
2. A tax on land or land values.
3. A tax on buildings.
4. A tax on vehicles or boats.
5. A tax on animals.
6. A tax on menials and domestic servants.
7. An octroi.
8. A terminal tax on goods imported into local areas in which the octroi was levied on or before the 6th July, 1917.
9. A tax on trades, professions and callings.
10. A tax on private markets.
11. A tax imposed in return for services rendered such as:

    (*a*) A water rate.
    (*b*) A lighting rate.
    (*c*) A scavenging, sanitary or sewage rate.
    (*d*) A drainage rate.
    (*e*) Fees for the use of markets and other public conveniences.

APPENDIX III

SPECIMEN OF A DEMAND

DEMAND NO. 1

CUSTOMS

Rs.73,17,000

	Actuals, 1922–23.		Budget Estimate, 1923–24.		Revised Estimate, 1923–24.		Budget Estimate, 1924–25.	
	Non-voted.	Voted	Non-voted.	Voted.	Non-voted.	Voted.	Non-voted.	Voted.
India	—	—	—	30,000	—	—	—	5,48,000
Madras . . .	5,06,911	6,98,144	5,51,600	7,05,400	4,90,900	7,25,100	5,54,600	7,49,400
Bombay . . .	91,012	24,88,085	1,59,000	27,25,000	1,64,000	23,94,000	1,22,000	27,48,000
Bengal . . .	94,003	19,81,604	97,000	21,05,000	67,000	20,89,000	1,00,000	21,99,000
Punjab . . .	38,543	—	23,000	—	23,000	—	23,000	—
Burma . . .	65,913	9,47,109	84,000	10,15,000	92,000	9,23,000	73,000	10,18,000
Bihar and Orissa . .	—	18,335	—	17,000	—	17,000	—	18,000
Central Provinces . .	—	770	—	2,000	—	2,000	—	2,000
Exchange . . .	21,882	23,047	27,000	18,000	24,000	38,000	21,000	35,000
For rounding . .	—	—	+400	−400	+100	−100	+400	−400
	8,18,264	61,57,094	9,42,000	66,17,000	8,61,000	61,88,000	8,94,000	73,17,000
Lump reduction made by the Assembly . .	—	—	—	−4,00,000	—	—	—	—
	8,18,264	61,57,094	9,42,000	62,17,000	8,61,000	61,88,000	8,94,000	73,17,000
Net Total . .	69,75,358		71,59,000		70,49,000		82,11,000	

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DEMAND NO. 1—*continued*

			Budget Estimate, Actuals, 1923–24.		Revised Estimate, 1923–24.		Budget Estimate, 1923–24.	
			Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
		INDIA.						
Pay of Officers' Allowances, Honoraries, etc.		Assistant Collectors . . .	—	30,000	—	—	—	—
		Overtime and holiday allowances	—	—	—	—	—	(*a*) 4,58,480*
Establishment charges payable to other Governments, Departments, etc.		**Cost of Collection of Customs duty on articles of Inward Foreign Letters and Parcels**	—	—	—	—	—	(*b*) 90,000
		For rounding . . .	—	—	—	—	—	—480
		Total (voted) . . .	—	30,000	—	—	—	5,48,000
		MADRAS. Sea Customs.						
Pay Officers	1	*Collector* (2,250,100—2,750) .	—	*28,200*	—	—	*30,600*	
,, ,,	2	*Assistant Collectors* (350–1,500)+ *Oversea Pay* (150–250) . .	—	*23,400*	—	—	*24,000*	
,, ,,	1	Assistant Collector (350–1,300),	—	7,200	—	—	8,400	
		Leave Salary . . .	—	1,300	—	—	—	
			22,769	—	—	*28,700*	—	
			—		60,100	—		63,000
			35,208	—	—	29,400	—	—

Pay of Establishment 269	Appraisers, Preventive Officers, Clerks, etc., at varying rates from Rs.15 to Rs.700) . .	—	*2,26,608*	—	—	2,29,152	—
	Temporary Establishment .	—	15,378	—	—	14,832	—
	Leave Salary	—	20,000	—	—	20,000	—
		2,52,354		2,61,986	2,48,500		2,63,984
Allowances and Honoraries, etc.	Travelling and tentage . .	—	9,600	—	—	9,600	—
	Rewards	—	4,000	—	—	4,000	—
	Overtime and Holiday Allowances	100	30,000	—	—	31,000	—
		44,029		43,600	42,000		44,600
Supplies and Services.	PURCHASE AND REPAIR OF BOATS	—	9,600	—	—	650	—
	Purchase of Comptometers .	—	—	—	—	(*c*) 3,400*	—
		351		650	500		4,050
Contingencies	Contract Contingencies . .	—	4,000	—	—	4,000	—
	Liveries and Clothing . .	—	10,00	—	—	1,000	—
	Rates and Taxes . . .	—	2,000	—	—	2,000	—
	Telephone Charges . . .	—	1,100	—	—	1,325	—
	Other Contingent Expenditure .	—	3,360	—	—	3,130	—
		11,694		11,460	12,500		11,455
Establishment charges payable to other Governments, Departments, etc.	Portion of charges of the Customs Establishment in the Board's Office	—		—			(*d*) 5,910
	For rounding . . .	—	—	+504	—		+1
	Total Sea Customs . .	3,66,505	—	3,78,300	3,61,600	—	3,93,000

New items of expenditure are printed in thick type.
Such of the items as have received the approval of Standing Finance Committee are marked with asterisk.
Not-voted items are printed in italics.

APPENDIX IV

RULES GOVERNING THE EXPENDITURE POWERS OF THE GOVERNMENT OF INDIA

Resolution from the Government of India, Finance Department, No. 1448–E.A., dated 29th September, 1922, as modified by resolution No. 518, Ex., dated the 2nd March, 1923:

His Majesty's Secretary for India in Council has been pleased to make the rules appended to this resolution, defining the classes of expenditure from central revenues upon subjects, other than provincial subjects, which the Governor-General in Council may not sanction without the previous consent of the Secretary of State in Council. These rules supersede all previous rules of a similar nature and, subject to their observance, orders regarding specific cases of expenditure passed by the Secretary of State in Council under regulations previously in force will no longer be binding.

"2. If the sanction of the Secretary of State in Council is required by these rules to any expenditure, such sanction should ordinarily be obtained before the Legislative Assembly is asked to vote supply to meet the expenditure. The Governor-General in Council may depart from this rule in cases of extreme urgency, where the time available is so short that sanction cannot be obtained by telegraph; but in such a case a statement showing all schemes for which supply has been asked before sanction has been obtained must be submitted to the Secretary of State as soon as possible after the presentation of the demands to the Assembly.

"3. The Governor-General in Council may sanction an excess over an estimate which has, prior to the introduction of these rules, received the sanction of the Secretary of State in Council if the total cost of the estimate, as increased by the excess, is within the powers of sanction conferred upon the Governor-General in Council by these rules; and may sanction the extension of a temporary post which has received similar sanction

if he would, under these rules, be competent to sanction the creation of such a post for the full term as extended.

"4. Subject to observance of these rules and to the provisions of Section 67 A of the Government of India Act, the Governor-General in Council has full power to sanction expenditure from central revenues upon subjects other than provincial subjects and, with the previous consent of the Finance Department, to delegate such power upon such condition as he may think fit either to any officer subordinate to him or to a Local Government acting as his agent in relation to a central subject. Any sanction given under this rule will remain valid for the specified period for which it is given, subject in the case of voted expenditure to the voting of supply in each year. Orders of delegation passed under this rule may contain a provision for delegation by the authority to which the powers are delegated."

Accompaniment to the above Resolution

Rules relating to expenditure by the Government of India on subjects other than provincial.

The previous sanction of the Secretary of State in Council is necessary :—

(1) To the creation of any new or the abolition of any existing permanent post, or to the increase or reduction of the pay drawn by the incumbent of any permanent post, if the post in either case is one which ordinarily be held by a member of one of the services named in the schedule, or to the increase or reduction of the cadre of any of those services or of a service ordinarily filled by officers holding the King's Commission.

(2) To the creation of a permanent post on a maximum rate of pay exceeding Rs.1200 a month, or the increase of the maximum pay of a sanctioned permanent post to an amount exceeding Rs.1200 a month.

(3) To the creation of a temporary post, on pay exceeding Rs.4000 a month, or the extension beyond a period of two years (or, in the case of a post for settlement operations, of five years) of a temporary post or deputation on pay exceeding Rs.1200 a month.

(4) To the grant to any Government servant or to the family or other dependents of any deceased Government servant of an allowance, pension or gratuity which is not admissible under

rules made or for the time being in force under section 96 B of the Government of India Act, or under Army Regulations, India, except in the following cases :—

(*a*) Compassionate gratuities to the families of Government servants left in indigent circumstances, subject to such annual limits as the Secretary of State in Council may prescribe ; and

(*b*) pensions or gratuities to Government servants wounded or otherwise injured while employed in Government service, or to the families of Government servants dying as the result of wounds or injuries sustained while employed in such service, granted in accordance with such rules as have been or may be laid down by the Secretary of State in Council in this behalf.

(5) To any expenditure on a measure costing more than Rs.5,00,000 (initial plus one year's recurring) and involving outlay chargeable to the Army or Marine estimates.

(6) (*a*) To any expenditure on the inception of a Military Rorks project which is estimated to cost more than Rs.10,00,000.

(*b*) To any expenditure on a Military works project in excess of the original sanctioned estimate if,

(i) the excess is more than 10 per cent of the original sanctioned estimate, and the estimated cost of the project thereby becomes more than Rs.10,00,000.

(ii) The original estimate has been sanctioned by the Secretary of State, and the excess is more than 10 per cent of that estimate or more than Rs.10,00,000.

(*c*) To any expenditure on a Military works project, in excess of a revised or completion estimate sanctioned by the Secretary of State.

Provided that, for the purposes of clauses (*b*) (ii) and (*c*) of the rule, if any section accounting for 5 per cent or more of the estimated cost of a project sanctioned by the Secretary of State is abandoned the estimated cost of the works in that section shall be excluded from the sanctioned estimate of the project for the purpose of determining whether the Secretary of State's sanction is necessary.

(7) To any expenditure on the purchase of imported stores or stationery, otherwise than in accordance with such rules

as may be made in this behalf by the Secretary of State in Council.

(8) To any expenditure, otherwise than in accordance with such rules as have been or may be laid down in this behalf by the Secretary of State in Council, upon—

(*a*) the erection, alteration, furnishing, or equipment of a church ; or a grant-in-aid towards the erection alteration, furnishing or equipment of a Church not wholly constructed out of Public Funds ; or

(*b*) the provision of additions to the list of special saloon and inspection railway carriages reserved for the use of high officials ; or

(*c*) the staff, household, and contract allowances, or the residences and furniture provided for the use of the Governor-General ; or

(*d*) railways.

2. The foregoing rules do not apply to expenditure in time of war with a view to its prosecution. The Government of India have full powers with regard to such expenditure, subject only to the general control of war operations which is exercised by the Secretary of State for India in consultation with His Majesty's Government ; to the necessity of obtaining the sanction of the Secretary of State in Council to really important special measures required to carry out those operations, where in the judgment of the Government of India time permits a previous reference to him and to the obligation to keep as fully informed as circumstances allow of their important actions.

The Schedule

(1) Indian Civil Service.
(2) Indian Police Service.
(3) Indian Forest Service.
(4) Indian Educational Service.
(5) Indian Agricultural Service.
(6) Indian Service of Engineers.
(7) Indian Veterinary Service.
(8) India Medical Service.
(9) Imperial Customs Service.
(10) Indian Audit and Accounts Service (Civil and Military).

(11) Superintendents and Class I of the Survey of India Department.
(12) The Superior Staff of the Geological Survey of India Department.
(13) The Superior Telegraph Branch of the Posts and Telegraphs Department.
(14) The State Railway Engineering Service.
(15) The Superior Staff of the Mint and Assay Departments.
(16) The Archæological Department.
(17) Any other service declared by the Secretary of State in Council to be included in this schedule.

Rules Governing Expenditure by Local Governments on Provincial Reserved Subjects

Resolution from the Government of India, Finance Department, No. 1449–E.A., dated 29th September, 1922, as amended by G.I.F.D. Resolution No. 2119 Ex, dated the 18th September, 1923 :—

"His Majesty's Secretary of State for India in Council has been pleased to make the rules appended to this Resolution, defining the classes of expenditure on reserved provincial subjects which a Governor in Council may not sanction without the previous consent of the Secretary of State in Council. These rules supersede all previous rules of a similar nature and, subject to their observance, orders regarding specific cases of expenditure passed by the Secretary of State in Council or the Governor-General in Council under regulations previously in force will no longer be binding.

"2. If the sanction of the Secretary of State in Council is required by these rules to any expenditure, such sanction should ordinarily be obtained before the Legislative Council is asked to vote supply to meet the expenditure. The Governor in Council may depart from this rule in cases of extreme urgency, where the time available is so short that sanction cannot be obtained by telegraph ; but in such a case a statement showing all schemes for which supply has been asked before sanction has been obtained must be submitted to the Secretary of State in Council as soon as possible after the presentation of the demands to the Council.

"3. The Governor in Council may sanction any excess over an estimate which has, prior to the introduction of these rules,

received the sanction of the Secretary of State in Council or the Governor-General in Council if the total cost of the estimates as increased by the excess, is within the powers of sanction conferred upon the Governor in Council by these rules ; and may sanction the extension of a temporary post which has received similar sanction the creation of such a post for the full term as extended.

"4. Subject to the observance of these rules and to the provisions of section 72D of the Government of India Act, the Governor in Council has full power to sanction expenditure upon reserved provincial subjects and, with the previous consent of his Finance Department, to delegate such power upon such conditions as he may think fit to any officer subordinate to him. Any sanction given under this rule will remain valid for the specified period for which it is given, subject, in the case of voted expenditure, to the voting of supply in each year."

Accompaniment to the above Resolution :—

Rules relating to expenditure by a Governor in Council on reserved provincial subjects.

1. The previous sanction of the Secretary of State in Council is necessary :—

(1) To the creation of any new or the abolition of any existing permanent post, or to the increase or reduction of the pay drawn by the incumbent of any permanent post, if the post in either case is one which would ordinarily be held by a member of an all-India Service or by an officer holding the King's Commission or to the increase or reduction of the cadre of an all-India Service.

(2) To the creation of permanent post on maximum rate of pay exceeding Rs.1200 a month, or in Burma Rs.1250 a month, or the increase of the maximum pay of a sanctioned permanent post to an amount exceeding Rs.1200 a month or in Burma Rs.1250 a month.

(3) To the creation of temporary post on pay exceeding Rs.4000 a month, or the extension beyond a period of two years (or, in the case of a post for settlement operations, of five years) of a temporary post or deputation on pay exceeding Rs.1200 a month in Burma Rs.1250 a month.

(4) To the grant to any Government servant or to the family

or other dependents of any deceased Government Servant of an allowance, pension or gratuity which is not admissible under rules made or for the time being in force under Section 96 B of the Government of India Act, except in the following cases :—

(*a*) Compassionate gratuities to the families of the Government servants left in indigent circumstances subject to such annual limits as the Secretary of State in Council may prescribe ; and

(*b*) pensions or gratuities to Government servants wounded or otherwise injured while employed in Government Service or to the families of Government servants dying as the result of wounds or injuries sustained while employed in such service, granted in accordance with such rules as have been or may be laid down by the Secretary of State in Council in this behalf.

(5) To any expenditure on the purchase of imported stores or stationery, otherwise than in accordance with such rules as may be made in this behalf by the Secretary of State in Council.

(6) To capital expenditure upon irrigation and navigation works including docks and harbours, and upon projects for drainage embankment and water storage and the utilization of water-power in any of the following cases, namely :—

(*a*) Where the project concerned materially affects the interests of more than one Local Government ;

(*b*) where the original estimate exceeds 50 lacs of rupees ;

(*c*) where a revised estimate exceeds by 15 per cent an original estimate sanctioned by the Secretary of State in Council ; and

(*d*) where a further revised estimate is proposed, after one revised estimate has already been sanctioned by the Secretary of State in Council.

(7) To a revision of permanent establishment involving additional establishment charges exceeding Rs.5 lacs a year ; provided that, if a resolution has been passed by the Legislative Council recommending an increase of establishment charges for this purpose, the sanction of the Secretary of State in Council shall not be required unless the expenditure so recommended exceeds 15 lacs a year.

(8) To any increase of the contract, sumptuary or furniture grant of a Governor.

(9) To expenditure upon original works on the residences of a Governor exceeding Rs.50,000 in any year. The Governor-General in Council shall, if necessary, decide whether a charge falls under the head of original works.

(10) To any expenditure upon railway carriages or water-borne vessels specially reserved for the use of high officials otherwise than in connection with the maintenance of such carriage or vessels already set apart with the sanction of the Secretary of State in Council for the exclusive use of a Governor.

2. (1) Every application for the sanction of the Secretary of State in Council required by Rule I shall be addressed to the Governor-General in Council, who shall, save as hereinafter provided, forward the same with his recommendations, and with such further explanations of the proposal as he may have seen fit to require from the Local Government, to the Secretary of State in Council.

(2) If the application relates—

(*a*) to the grant in an individual case of any increase in pay, or

(*b*) To the creation of or extension of a temporary post, the Governor-General in Council may, at his discretion, on behalf of the Secretary of State in Council, sanction the proposal, or may, and, if he dissents from the proposal, shall forward the application with his recommendations, and with such further explanations of the proposal as he may have seen fit to require from the Local Government, for the orders of the Secretary of State in Council.

APPENDIX V

EXTRACT FROM TREASURY ORDERS ISSUED BY THE GOVERNOR-GENERAL IN COUNCIL WITH THE PREVIOUS CONSENT OF THE SECRETARY OF STATE IN COUNCIL UNDER RULE 16 OF THE DEVOLUTION RULES

Section IV.—General system of Treasury control.

4. Unless in any case the Governor in Council, with the concurrence of the Auditor-General, otherwise direct, there shall be in every district a treasury under the charge of a treasury officer. If moneys standing in the public account are, in any district, not deposited in the Bank, the treasury of that district shall be divided into two departments: that of the accounts, under the charge of an accountant, and that of the cash, under the charge of a treasurer.

5. In any treasury in which a Government servant of the Indian Audit Department has not been appointed, as such, to be treasury officer, the following orders will supply :—

(*a*) The Treasury shall be in the general charge of the Collector, who may entrust the immediate executive control to a treasury officer subordinate to him but may not divest himself of administrative control. He shall be responsible for the proper observance of these orders and for the punctual submission of all returns required from the Treasury by the Governor-General in Council.

(*b*) The duty of verifying and certifying the monthly cash balance, if any, in the Treasury, and of submitting monthly accounts in such form or forms and after such verification as the Auditor-General may prescribe, shall be undertaken by the Collector or by such other officer as the Governor in Council may specify. It must be performed by the Collector in person at least once in every period of six months.

(c) A change of the incumbent of the office of Collector shall at once be reported to the principal Auditor concerned by the incoming Collector, who shall certify to the principal Auditor the amount of the cash balance, if any, which he has taken over. The certificate shall be submitted in such form and after such verification as the Auditor-General may prescribe.

6. In any Treasury in which a Government servant of the Indian Audit Department has been appointed, as such, to be treasury officer, the duties of the Collector, in relation to the custody of moneys in the Treasury shall be such as the Governor in Council, with the concurrence of the Governor-General in Council, may specify.

Section V.—Payment of Government moneys into the public account.

7. Except as provided in order 8, all moneys received by Government servants in their official capacity, other than moneys withdrawn from the public account under the provisions of Section VIII below, shall without undue delay be paid in full into a Treasury or into the bank and shall be included in the general balances of Government. Departmental receipts shall not be appropriated to meet departmental expenditure except with the sanction of the Governor-General in Council.

8. In certain exceptional cases, Government servants may be permitted to open a separate account with a bank and to pay into it moneys received by them in their official capacity. The conditions on which such permission may be given are detailed in Appendix A.

9. (a) The procedure to be adopted by Government servants in paying into treasuries moneys derived from sources of provincial revenue and by treasuries in receiving such moneys and granting receipts for them shall be such as may be specified by the Governor in Council, with the concurrence of the Auditor-General.

(b) The procedure to be adopted by Government servants in paying into treasuries moneys not derived from sources of provincial revenue and by treasuries in receiving such moneys and granting receipts for them shall be such as may be specified by the Governor-General in Council.

(*c*) The procedure to be adopted by Government servants in paying moneys into the bank and by the bank in receiving such moneys and granting receipts for them shall be such as may be specified by the Governor-General in Council.

Section VI.—Custody of moneys standing in the public account.

10. (*a*) The procedure for the safe custody of moneys in a Treasury shall be such as the Governor in Council, with the concurrence of the Governor-General in Council, may specify.

(*b*) The bank is responsible for the safe custody of Government moneys deposited in the bank.

Section VII.—Transfer of moneys standing in the public account.

11. The transfer of Government moneys from one treasury to another, and between the currency chest balance and treasury balance of a treasury and between a treasury and the bank shall be governed by such instructions as the Controller of the Currency may issue in this behalf. It shall not be subject to the orders in Section VIII below.

Section VIII.—Withdrawal of moneys from the public account.

12. Definition.—In this section withdrawal means the withdrawal of funds from the public account for expenditure on provincial subjects. The procedure to be adopted by Government servants in withdrawing funds from the public account for expenditure on central subjects shall be such as may be specified by the Governor-General in Council.

13. General Rule.—Unless in any case the Governor in Council with the concurrence of the Auditor-General, otherwise direct, moneys may not be withdrawn from the public account without the written permission of the Treasury Officer or of a Government servant of the Indian Audit Department authorized in this behalf by the Auditor-General.

14. Power of a principal auditor.—A principal auditor may, subject to the general control of the Auditor-General, permit withdrawal for any purpose.

15. Instructions to the Treasury Officers.—(*a*) A Treasury Officer may permit withdrawal for the following purposes :—

(i) To pay sums due by Government to the drawing officer.

(ii) To place the drawing officer in funds to meet claims likely to be presented against Government in the immediate future by

(1) other Government servants or

(2) private parties.

(iii) To enable the drawing officer to supply funds to another Government servant from which to meet similar claims.

(iv) To pay direct from the Treasury sums due by Government to a private party.

(*b*) Unless in any case it be otherwise expressly ordered by a principal auditor, a Treasury Officer shall not permit withdrawal for any purpose not specified in clause (*a*) of this order.

16. Except as provided in orders 23 and 24 below, a Treasury Officer shall not permit withdrawal for any purpose unless the claim for withdrawal is presented by such person and in such form, and has been satisfactorily submitted by the Treasury Officer to such checks, as the Governor in Council, with the concurrence of the Auditor-General, may specify.

17. A Treasury Officer shall not honour a claim which he considers to be disputable. He shall require the claimant to refer it to the principal auditor responsible for the audit of the payment.

18. Except under the general or special orders of the Governor in Council, a payment shall be made in the district in which the claim arises.

19. The leave salary of a gazetted Government servant, who draws his leave salary in India, may be paid in any district in India. The leave salary of a non-gazetted Government servant may be paid in that district only in which his pay could be drawn if he were on duty.

20. Pensions payable in India may be paid in any district in India.

21. No withdrawal shall be permitted in order to meet the pay, leave salary or allowance of a gazetted Government ser-

vant, or a reward or honorarium payable to a gazetted Government servant, or any pension payable from the general revenues, until an Audit Officer has intimated the rate at which payment should be made.

22. No withdrawal shall be permitted in order to meet the first of any series of payments in a district of pay or allowances to a Government servant, other than a person newly appointed to Government service, unless the claim be supported by a last-pay certificate in such form as may be prescribed by the Auditor-General.

23. In case of urgent necessity, a Collector may require a Treasury Officer to make a payment in contravention of orders 16, 17, 18, 19, 21, or 22 above; provided that the Collector records an order in writing and immediately sends a copy of the order, together with an explanation of the circumstances which rendered it necessary, to the principal auditor who will audit the payment. The Treasury Officer also shall intimate the payment to the principal auditor.

24. A Treasury Officer may correct an arithmetical inaccuracy or an obvious mistake in any bill presented to him for payment, provided that he intimates to the drawing officer the correction which he makes.

25. Instructions to drawing officers.—A Government servant who is authorized to withdraw moneys by means of cheques shall notify to the Treasury Officer or to the local officials of the bank, as the case may be, the numbers of the cheque books which from time to time he proposes to use and of the cheques, which they contain.

26. When a Government servant who is authorized to draw or countersign cheques or bills payable at a treasury or the bank makes over charge of his office to another, he must send a specimen of the relieving Government servant's signature to the Treasury Officer or the local officials of the bank, as the case may be.

Section IX.—Responsibility for moneys withdrawn.

27. (*a*) A Government servant supplied with funds for expenditure shall be responsible for such funds until an account of them has been rendered to the satisfaction of the principal auditor concerned. In cases in which the acquittances of the

actual payees are not sent for audit the Government servant supplied with funds shall be held personally responsible for seeing that payments are made to the persons entitled to receive them.

(*b*) If any doubt arises as to the identity of the Government servant by whom an account of such funds shall be rendered, it shall be decided by the Governor in Council.

28. A Treasury Officer receiving an intimation from an Audit Officer that moneys have been incorrectly withdrawn, and that a certain sum should be recovered from a drawing officer, must affect the recovery without delay and without regard to any correspondence undertaken or contemplated with reference to the retrenchment order; and the drawing officer must without delay repay the sum by such method as the Audit Officer may prescribe.

Section X.—General Exception.

29. A Governor in Council may not, without the sanction of the Governor-General in Council, so exercise any power conferred upon him by these orders as to impose upon the bank in connection with Government business any responsibility which the bank is not liable to undertake at the time when these orders come into force.

APPENDIX VI

LIST OF MAJOR HEADS OF REVENUE AND EXPENDITURE

Section letters	Major heads and sections
	REVENUE.
A	PRINCIPAL HEADS OF REVENUE
	I. Customs.
	II. Taxes on Income.
	III. Salt.
	IV. Opium.
	V. Land Revenue.
	VI. Excise.
	VII. Stamps :
	(*a*) Non-judicial.
	(*b*) Judicial.
	VIII. Forest.
	IX. Registration.
	(*a*) Scheduled Taxes.
	X. Tributes from Indian States.
B	RAILWAYS.
	XI. State Railways :
	Gross receipts.
	Deduct working expenses.
	Surplus profits and net earnings paid to Companies.
	Net receipts.
	XII. Subsidized Companies.
C	IRRIGATION ; NAVIGATION, EMBANKMENT AND DRAINAGE WORKS.
	XIII. Irrigation, Navigation, Embankment and Drainage Works for which capital accounts are kept.
	(*a*) Irrigation Works :
	(1) Productive Works :
	Gross receipts.
	Direct receipts.
	Portion of land revenue due to irrigation.
	Deduct working expenses.
	Net receipts or payments.
	Total net receipts.
	(*b*) Navigation, Embankment, and Drainage Works :
	(Same heads as for Irrigation Works.)
	XIV. Irrigation, Navigation, Embankment, and Drainage Works, for which no capital accounts are kept.
	(*a*) Irrigation Works :
	(1) Works for which only revenue accounts are kept :
	Direct receipts.
	Deduct refunds.
	(2) Works for which neither capital nor revenue accounts are kept.
	Direct receipts.
	Deduct refunds.
	(*b*) Navigation, Embankment and Drainage Works :
	(Same heads as for (*a*).)
D	POSTS AND TELEGRAPHS.
	XV. Post and Telegraphs.
	Gross receipts.
	Deduct working expenses.
	Net receipts.
E	DEBT SERVICES.
	XVI. Interest.
F	CIVIL ADMINISTRATION.
	XVII. Administration of Justice.
	XVIII. Jails and Convict Settlements.

Section letters — Major heads and sections

XIX. Police.

XX. Ports and Pilotage.
(a) Major Ports.
(b) Minor Ports.

XXI. Education:
(a) University.
(b) Secondary.
(c) Primary.
(d) Special.
(e) General.

XXII. Medical.

XXIII. Public Health.

XXIV. Agriculture.

XXV. Industries.

XXVI. Miscellaneous Departments.

G CURRENCY AND MINT.

XXVII. Currency.

XXVIII. Mint.

H CIVIL WORKS.

XXIX. Civil Works.

XXX. Waterways and Embankments.

J MISCELLANEOUS.

XXXI. Transfers from Famine Insurance Fund.

XXXII. Receipts in aid of Superannuation.

XXXIII. Stationery and Printing.

XXXIV. Miscellaneous.

K MILITARY RECEIPTS.

XXXV. Army.
(a) Standing Army effective.
(b) Auxiliary and Territorial Forces.
(c) Non-effective.

XXXVI. Marine:
(a) Effective.
(b) Non-effective.

XXXVII. Military Works.

L PROVINCIAL CONTRIBUTIONS AND MISCELLANEOUS ADJUSTMENTS BETWEEN CENTRAL AND PROVINCIAL GOVERNMENTS.

Section letters — Major heads and sections

XXXVIII. Contributions to the Central Government by Provincial Governments.

XXXIX. Miscellaneous Adjustments between the Central and Provincial Governments.

BB RAILWAYS CAPITAL ACCOUNT NOT CHARGED TO REVENUE.

XL. Capital contributed by Railway Companies and Indian States towards outlay on State Railways.

HH CIVIL WORKS AND MISCELLANEOUS PUBLIC IMPROVEMENTS NOT CHARGED TO REVENUE.

XLI. Bombay Development Scheme.

EXPENDITURE.

A DIRECT DEMANDS ON THE REVENUE.

1. Customs.
2. Taxes on Income.
3. Salt.
4. Opium.
5. Land revenue.
6. Excise.
7. Stamps.
   (a) Non-judicial.
   (b) Judicial.
8. Forest.
9. Registration.
   (a) Scheduled taxes.

B RAILWAY REVENUE ACCOUNT.

10. State Railways:
    Interest on capital contributed by Companies and Indian States.
    Annuities in purchase of Railways.
    Sinking funds.
    Interest chargeable against Companies on advances.
    Interest on capital deposited by Companies.

Section letters	Major heads and sections
	11. Subsidized Companies.
	12. Miscellaneous Railway expenditure.
BB	RAILWAY CAPITAL ACCOUNT (CHARGED TO REVENUE).
	13. Construction of Railway.
C	REVENUE ACCOUNT OF IRRIGATION, NAVIGATION, EMBANKMENT AND DRAINAGE WORKS
	14. Interest on works for which capital accounts are kept.
	Irrigation works.
	Navigation, Embankment and Drainage Works.
	15. Other revenue expenditure financed from ordinary revenues.
	(*a*) Irrigation Works.
	(1) Works for which only revenue accounts are kept.
	(2) Works for which neither capital nor revenue accounts are kept.
	(3) Miscellaneous expenditure.
	(*b*) Navigation, Embankment, and Drainage Works.
	(Same head as for (*a*).)
	Deduct amount financed from ordinary revenues.
	16. (1) Other revenue expenditure financed from Famine Insurance grants.
	Irrigation works.
	Navigation, Embankment and Drainage Works.
CC	CAPITAL ACCOUNT OF IRRIGATION, NAVIGATION, EMBANKMENT AND DRAINAGE WORKS.
	17. Construction of Irrigation, Navigation, Embankment and Drainage Works.
	(*a*) Financed from Famine Insurance grants.
	Irrigation Works.
	Navigation, Embankment and Drainage Works.
	(*b*) Financed from ordinary revenues.
D	POSTS AND TELEGRAPHS REVENUE ACCOUNT.
	18. Posts and Telegraphs.
DD	POSTS AND TELEGRAPHS CAPITAL ACCOUNT (CHARGED TO REVENUE).
	19. Capital outlay on Posts and Telegraphs.
	Debt Services:
	20. Interest on ordinary debt.
	21. Interest on other obligations.
	22. Sinking funds.
F	CIVIL ADMINISTRATION.
	23. General administration:
	(*a*) Heads of provinces (including Governor-General), Executive Councils and Ministers.
	(*b*) Legislative bodies.
	(*c*) Secretariat and Headquarters' Establishments.
	(*d*) Commissioners.
	(*e*) District administration.
	(*f*) Miscellaneous.
	24. Audit.
	25. Administration of Justice.
	26. Jails and Convict Settlements.
	27. Police.
	28. Ports and Pilotage:
	(*a*) Major Ports.
	(*b*) Minor Ports.
	29. Ecclesiastical.
	30. Political.
	31. Scientific Department.
	32. Education:
	(*a*) University.
	(*b*) Secondary.
	(*c*) Primary.
	(*d*) Special.
	(*e*) General.

Section letters	Major heads and sections
	33. Medical.
	34. Public Health.
	35. Agriculture.
	36. Industries.
	37. Aviation.
	38. Miscellaneous departments.
G	CURRENCY AND MINT.
	39. Currency.
	40. Mint.
H	CIVIL WORKS.
	41. Civil works.
	42. Waterways and embankments.
J	MISCELLANEOUS.
	43. Famine Relief and Insurance :
	(*a*) Famine Relief.
	(*b*) Transfers to Famine Insurance fund.
	44. Territorial and Political pensions.
	45. Superannuation allowances and pensions.
	46. Stationery and pensions.
	47. Miscellaneous.
K	MILITARY SERVICE.
	48. Army :
	(*a*) Standing Army :
	Effective.
	Non-effective.
	(*b*) Auxiliary and Territorial forces :
	Effective.
	Non-effective.
	49. Marine :
	Effective.
	Non-effective.
	50. Military works.
L	PROVINCIAL CONTRIBUTIONS AND MISCELLANEOUS ADJUSTMENTS BETWEEN CENTRAL AND PROVINCIAL GOVERNMENTS.
	51. Contributions to the Central Government by Provincial Governments.
	52. Miscellaneous adjustments between the Central and Provincial Governments.

CAPITAL EXPENDITURE NOT CHARGED TO REVENUE.

Section letters	Major heads and sections
AA	PRINCIPAL REVENUE HEADS.
	52(*a*). Forest capital outlay.
BB	RAILWAY CAPITAL ACCOUNT NOT CHARGED TO REVENUE.
	53. Construction of State Railways.
	54. Redemption of liabilities involved in purchase of Railways.
CC	CAPITAL ACCOUNT OF IRRIGATION, NAVIGATION, EMBANKMENT AND DRAINAGE WORKS NOT CHARGED TO REVENUE.
	55. Construction of Irrigation, Navigation, Embankment and Drainage Works :
	(*a*) Irrigation Works :
	(1) Productive.
	(2) Unproductive.
	(*b*) Navigation, Embankment and Drainage works :
	(Same heads as for (*a*).)
	Deduct amount financed from Famine Insurance grants.
	Deduct amount financed from ordinary revenue.
	Add repayments of capital expenditure charged to ordinary revenue.
	Net amount not charged to revenue.

Section letters	Major heads and sections
DD	POSTS AND TELEGRAPHS CAPITAL ACCOUNT NOT CHARGED TO REVENUE.
	56. Capital outlay on Posts and Telegraphs.
FF	CIVIL ADMINISTRATION.
	56 (*a*). Capital outlay on improvement of public health.
	56 (*b*). Capital outlay on agricultural improvements.
	56 (*c*). Capital outlay on industrial development.
	56 (*d*). Capital outlay on hydro-electric schemes
HH	CIVIL WORKS AND MISCELLANEOUS PUBLIC IMPROVEMENTS NOT CHARGED TO REVENUE.
	57. Initial expenditure on new capital at Delhi.
	58. Bombay development scheme.
	59. Civil works not charged to revenue.
JJ	MISCELLANEOUS CAPITAL EXPENDITURE NOT CHARGED TO REVENUE.
	59 (*a*). Other provincial works not charged to revenue.

APPENDIX VII

"The following rules govern the allocation of railway expenditure between Capital and Revenue.

1. Capital bears all charges for the first construction and equipment of project as well as charges for maintenance on sections not opened for working, and charges for such subsequent additions and improvements as may be admitted by competent authority.

2. An addition or improvement admit of the cost being charged to Capital must be a permanent enlargement and substantial improvement in the character and object of the existing imperfect structure.

3. Revenue bears all charges for maintenance and working expenses which embrace all expenditure for the working and upkeep of the railway, for alterations, and for such minor additions and improvements as it may be considered desirable to charge to Revenue instead of increasing the capital cost of the railway.

NOTE.—Sidings required purely for Revenue purposes, e.g. ballast and fuel sidings, are chargeable to Revenue and not to Capital.

4. New minor works costing Rs.2000 and under chargeable to Revenue.

5. If any extraordinary casualty should occur, such as the destruction of bridge by flood, the case may be regarded as exceptional, and the cost of construction or replacement will be charged to capital or Revenue or divided between them as may be deemed proper by the Railway Board according to the circumstances of the case.

6. In the case of renewals and replacements of existing works involving improvements, if the estimated cost of the new work is less than the cost of the original work, or below the new minor works limit of Rs.2000, the whole cost of the new work will be charged to Revenue and that of the original work will be left at the debit of Capital. In other cases the whole cost of new work will be charged to Capital, and that of the original work

which may be estimated if the actual original cost is not known, will be written back from Capital to Revenue.

7. The allocation of the cost of temporary works which are incidental to other works should follow that of the main works in connection with which they are required, and where the main works are debitable partly to the Capital and partly to Revenue, their cost should be divided between the two in rateable proportions. This applies to temporary diversions.

8. The cost of purely temporary or experimental work on an open line is chargeable to Revenue, but it may be subsequently transferred to Capital if the work is permanently adopted.

Note.—In the case of trial stations, if the estimated cost is within the limit for new minor works (which should generally be the case for a true trial station the necessity for which is at all open to doubt), the amount should be charged against the Revenue Account, but if the cost exceeds that limit the amount should be charged against the Capital Account. If, however, the station is hereafter abandoned the expenditure should be written back to Revenue.

9. Except as provided for by paragraph 35 II (*b*), all charges for land taken up permanently, irrespective of the amount of cost or whether required for Capital or Revenue, works are debitable to Capital under the main head II.—Land. Rent or other miscellaneous charges in connection with hire of land should be charged to the work or purpose concerned.

10. In the case of light rails being renewed with heavier rails, Capital may be charged with a portion of the cost of the new material proportionate to the excess weight by which the new rails exceeds the old rails, subject to the proviso that such charge to Capital shall never exceed the actual excess on the cost of the new materials over the original cost of the old.

Note.—In cases in which renewal of track by a different weight of rail and different type of sleeper is proposed, the debit to Capital should be arrived at by estimating the original cost of the material in the track to be renewed and the cost at present prices of similar material, and deducting whichever is greater from the cost of the new material which it is proposed to use.

11. In connection with estimates for the strengthening and renewing of bridges the allocation of the cost of each bridge should be considered separately on the following basis :—

(*a*) Where old girders are replaced by new and heavier ones, Capital should only be charged with a portion of the cost of the new material, proportionate to the excess weight of the new over the old girders, or with the difference in cost of the new material over the original cost of the old, whichever is less, the balance of cost together with the charges for dismantling and re-erecting should be debited to Revenue which will receive credit for the present value of the materials returned. The fact that the girders are not entirely worn out but are only renewed on account of increased loads, would be provided for by the larger credit to Revenue for old girders.

(*b*) Where any of the released girders are subsequently used in duplicating other spans, Capital should bear the cost of the second pair of girders at their present value as credited to Revenue. But the total charge to Capital when released girders are used in duplicating shall in no case exceed the charge that would be made to Capital if the old girders were replaced by new ones of the necessary strength.

(*c*) Similarly where the strengthening of bridges takes the form of increased weight of material added to the existing girders in preference to replacing the girders with new ones of the necessary strength, the charge of Capital in respect of the new materials may not exceed the charge that would be made to Capital if the old girders were replaced by new ones of the necessary strength.

(*d*) Raising the road bed in the approaches of railway bridges necessitated by the replacement of girders, originally erected by others of greater depth, is not in itself an improvement, but is an essential part of the improvement effected by introducing deeper girders. Accordingly the cost of the additional earthwork carried out in raising the road level is chargeable to Capital provided that the deeper girders give stronger bridges.

12. In all cases the renewals, all charges on account of freight of materials from depot to site and loading and unloading of materials should be debited wholly to Revenue."

(Para. 47 of the State Railway Code for the Engineering Department, first edition, 1921.)

APPENDIX VIII

EXTRACT FROM AUDITOR-GENERAL'S RULES FRAMED BY THE SECRETARY OF STATE IN COUNCIL UNDER SECTION 96 D (I) OF THE GOVERNMENT OF INDIA ACT

Duties and powers.—Subject to any general or special orders of the Secretary of State in Council, the Auditor-General shall be :—

(i) the final audit authority in India ; and

(ii) responsible for the efficiency of the audit of expenditure in India from the revenues of India.

He shall further be, to the extent authorized by these rules, the administrative head of the Indian Audit Department.

9. The Auditor-General shall have authority—

(i) to inspect, either personally or by his Deputy Auditors-General, any office of accounts and audit in India ;

(ii) to arrange for test audit of any office of accounts ;

(iii) subject to any orders of the Secretary of State in Council prescribing the nature and extent of the audit to be applied to specified classes of expenditure, to frame rules in all matters pertaining to audit ; particularly in respect of the method and extent of audit and the raising and pursuance of objections ;

(iv) to instruct the head of an excluded audit department to arrange for the submission of accounts to the Auditor-General in such form and at such time as the Auditor-General may prescribe ; and

(v) to pass orders as regards the conduct of business within, and the administration, organization, and discipline of, the office of accounts and audit in India other than those which form part of an excluded audit department.

Duties and powers as regards audit.—10. (*a*) The Auditor-General, without prejudice to his other audit functions, is

responsible that audit is conducted with reference to the following canons namely—

(1) Every public officer should exercise the same vigilance in respect of expenditure incurred from Government revenues as a person of ordinary prudence would exercise in respect of the expenditure of his own money.

(2) Money borrowed on the security of allocated revenues should be expended on those objects only for which, as provided by rules made under the Act, money may be so borrowed.

If the money is utilized on works which are not productive, arrangements should be made for the amortization of the debt.

(3) No authority should exercise its powers of sanctioning expenditure to pass an order which will be directly to its own advantage.

(4) Government revenues should not be utilized for the benefit of a particular person or section of the community unless—

(i) the amount of expenditure involved is insignificant, or

(ii) a claim for the amount could be enforced in a court of law, or

(iii) the expenditure is in pursuance of a recognized policy or custom.

(5) No authority should sanction any expenditure which is likely to involve at a later date expenditure beyond its own powers of sanction.

(6) The amount of allowances, such as travelling allowances granted to meet expenditure of particular type, should be so regulated that the allowances are not on the whole sources of profit to the recipients.

(*b*) The Auditor-General or any principal auditor should bring to the notice of the Governor-General in Council or the Local Government, as the case may be, any breach of one of these canons.

11. The audit of sanction to expenditure accorded by the Governor-General in Council be under the immediate supervision of the Auditor-General, who shall when he accepts such sanctions, communicate his acceptance to the audit officer who will audit the expenditure against the sanctions.

12. The Auditor-General shall, if so required by the Governor-General in Council,

(i) arrange for the audit of the accounts of the receipts of revenue of any Government department, the accounts of any public or quasi-public body, or any other accounts although they may not relate directly to the receipt and expenditure of Government moneys ; and

(ii) arrange for the audit of stores or stock in the possession of an officer or a department of Government, and for the audit of grants of land and alienations of land revenue.

13. If the Auditor-General considers it desirable that the whole or any part of the audit applied to Government accounts or to any other accounts which he is required to audit under Rule 12, shall be conducted in the offices in which these accounts originate, he may require that these accounts together with all books, papers, and writing having relation thereto, shall at all convenient times be made available in those offices for inspection by his audit officers.

14. When an objection taken in the course of audit cannot be adjusted by a principal auditor in consultation with the authorities concerned, the Auditor-General may either instruct the principal auditor to withdraw the objection or require the Governor-General in Council or the Local Government concerned to obtain the requisite sanction or in default, to recover the amount under objection :

Provided that (i) if the objection to any expenditure is based solely on the ground that such expenditure contravenes one of the canons set out in Rule 10 above the Auditor-General or principal auditor shall withdraw such objection, at the request of the Finance Department of the Government concerned, if the Finance Department states that the breach of canons and the action taken thereon by the Government will be reported as soon as possible to the Committee on Public Accounts, and (ii) if the Governor-General in Council or the Local Government as the case may be, orders in writing that the recovery of the amount under objection shall be foregone, the Auditor-General or principal auditor shall withdraw such objection, but may require that the action taken shall be reported to the Committee on Public Accounts.

15. (*a*) The Auditor-General shall on such dates as he may prescribe, obtain from each principal auditor and from any

officers of the Indian Audit Department to whom he may entrust this duty, Audit and Appropriation Reports reviewing the result of the audit conduct by and under such officer during the past official year. Any officer of Government may be called upon to provide any information necessary for the preparation of these reports, which shall be in such form and shall deal with such matters as the Auditor-General may prescribe. On receipt of these the Auditor-General shall transmit them to the Governor-General in Council or to the Finance Department of the Local Government concerned with such comments as he may think fit.

(*b*) The Auditor-General shall forward to the Secretary of State through the Governor-General in Council the several reports dealing with the total expenditure in India in each year with his detailed comments on each report and may also offer such further comments of a general nature as he may think fit.

16. (*a*) The Auditor-General may on his own motion, and shall, on reference being made to him by the Governor-General in Council or by a Local Government, review any audit decision of any audit officer, and, if he thinks fit, overrule it.

(*b*) The Auditor-General may dispense with a previous reference to the Secretary of State in Council, otherwise required by the rules regarding sanction to expenditure from time to time in force, in cases where in his opinion the failure to obtain the sanction of the Secretary of State in Council involves a breach of the letter rather than of the spirit of the rules.

17. The Auditor-General shall have power to require that any books, papers or writings relating to the accounts audited by any audit department in India shall be sent for inspection by him or by any other officer of the Indian Audit Department: provided that :—

(i) If the Governor-General in Council or the Local Government, as the case may be, certifies that the documents in question are secret, the Auditor-General or other officer, as the case may be, shall accept, in lieu of such documents and as a correct account of the facts stated therein, a statement certified by the Governor-General in Council or the Local Government; and

(ii) if the documents are confidential, the officer to whom they are made over shall be responsible for preventing disclosure of their contents.

Duties and powers as regards accounts.

18. The Auditor-General shall compile the Finance and Revenue Accounts of India in such form as may from time to time be prescribed by the Secretary of State in Council and shall send them to the Governor-General in Council for transmission to the Secretary of State in Council. He may call upon any Government officer to furnish any information in such form as may be required for the completion of these accounts.

19. The Auditor-General shall have power to prescribe the forms in which accounts shall be kept in audit offices: provided that no change which will affect the form of the Finance and the Revenue Accounts shall be made without the previous sanction of the Secretary of State in Council.

20. If a doubt or a dispute arises as to the major head under which a particular minor head, or as to the minor head under which a particular detailed head should be included, it shall be decided by the Auditor-General.

21. The Auditor-General shall prepare in each year a review of the balances of the books maintained by the Audit departments and shall send it to the Governor-General in Council for submission to the Secretary of State in Council.

22. The Auditor-General shall have power to determine the form in which officers rendering accounts to the Indian Audit Department shall render such accounts and in which the initial accounts, from which the accounts so rendered are compiled, or on which they are based, shall be maintained.

23. The Auditor-General shall supply, or shall arrange that officers subordinate to him, supply any information required by the Governor-General in Council or by a Local Government which can be derived from the accounts maintained in the offices under his control.

24. The Auditor-General shall arrange that such assistance as may be required shall be rendered by the officers of the Indian Audit Department to the Governor-General in Council, the Local Governments and authorities in the preparation of their annual budget estimates.

APPENDIX IX

SEPARATION OF RAILWAY FROM GENERAL FINANCE

On the 20th September, 1924, the Legislative Assembly adopted an amended resolution regarding the separation of railway from general finance. The resolution was originally moved by Sir Charles Innes—the Commerce Member of the Government of India—on the 3rd March, 1924. The proposal was, however, referred to a committee and its discussion postponed. The committee worked out the details and submitted its report. There were some changes in the form of the resolution, and one or two in its substance. The resolution was redrafted generally in order to remove certain misconceptions and bring out the intention of the Government more clearly. There was not much difference of opinion regarding the underlying principle of the proposal. But the amendment moved by Sir Parshotamdas Thakurdas, which provided against the transference of the management of the state railways to the companies, and for the rapid Indianization of the services, gave rise to an animated debate. It looked as if this important measure of financial reform was going to be wrecked in the heated atmosphere of the Assembly, but the good sense of the House asserted itself, and saved the situation. The consideration of the measure was adjourned for a day. The next day a compromise acceptable to all the parties was arrived at, and the amended resolution was duly carried. The text of the resolution as finally adopted by the Legislative Assembly is given in the footnote.[1]

[1] "The Assembly recommends to the Governor-General in Council that in order to relieve the general budget from the violent fluctuations caused by the incorporation therein of the railway estimates and to enable railways to carry out a continuous railway policy based on the necessity of making a definite return to the general revenues on the money expended by the State on railways:

(1) The railway finances shall be separated from the general finances of the country, and the general revenues shall receive a definite general contribution which shall be the first charge on the net receipts of railways.

(2) The contribution shall be based on capital at charge and working

It is generally admitted that the separation of the railway from the general finance is in the interest of the railways, the country as a whole, and the tax-payer. The Acworth Committee declared themselves in favour of the separation in the following words which are both emphatic and clear: "We do not believe," they wrote in the para. 58 of their Report, "that it is possible to fit the railway management into the rigid framework of the existing financial system of the Government of India. We do not think that the Indian railways can be modernized, improved, and enlarged so as to give to India services of which it is in crying need at the moment, nor can the

results of the commercial lines (excluding the capital contributed by companies and Indian States) at the end of the penultimate financial year plus one-fifth of any surplus profits remaining after payment of the fixed return, subject to the condition, that if in any year railway revenues are insufficient to provide the percentage of one per cent on the capital at charge, surplus profits in the next or subsequent years will not be deemed to have accrued for purposes of division until such deficiency has been made good.

The interest on the capital at charge of, and loss in working strategic lines shall be borne by the general revenues, and shall consequently be deducted from the contribution calculated in order to arrive at the net amount payable from railway to general revenue every year.

(3) Any surplus remaining after the payment to general revenues shall be transferred to a railway reserve; provided that if the amount available for transfer to the railway reserve exceeds in any year three crores of rupees, two-third of excess over three crores shall be transferred to railway reserve and the remaining one-third shall accrue to general revenues.

(4) The railway reserve shall be used to secure the payment of general contribution to general revenues; to provide, if necessary, for arrears of depreciation and for writing down and writing off capital: and to strengthen the general position of railways in order that services rendered to the public may be improved and the rates may be reduced.

(5) The railway administration shall be entitled, subject to such conditions as may be prescribed by the Government of India, to borrow temporarily from the capital or from the reserve for the purposes of meeting expenditure for which there is no provision or insufficient provision in the revenue budget subject to the obligation of making repayments of such borrowings out of the revenue budget of the subsequent years.

(6) A Standing Finance Committee for Railways shall be constituted, consisting of one nominated official member of the Legislative Assembly, who should be chairman, and eleven members elected by the Legislative Assembly from their body. The members of the Standing Finance Committee for Railways shall be ex officio members of the Central Advisory Council, which shall consist, in addition, of not more than one further nominated official member, six non-official members selected from a panel of eight elected by the Council of State from their body, and six non-official members selected from a panel of eight elected by the Legislative Assembly from their body.

The Railway Department shall place the estimate of the railway

railways yield to the Indian public the financial return which they are entitled to expect from so valuable a property until the whole financial methods are radically reformed. The essence of the reform is contained in two things, (1) the complete separation of railway budget from the general budget of the country, and its reconstruction which will free a great commercial business from the trammels of a system which assumes that the concern goes out of business on the 31st March and recommences *de novo* on the 1st of April; and (2) the emancipation of the railway management from the control of the Finance Department." The recommendations of the

expenditure before the Standing Finance Committee for Railways on some date prior to the date of the discussion of the demand for grants for railways, and shall, as far as possible, instead of expenditure programme revenue, show the expenditure under a depreciation fund created as per the new rules for charge to capital and revenue.

(7) The railway budget shall be presented to the Legislative Assembly, if possible, in advance of the general budget, and separate days shall be allotted for its discussion, and the Member in charge of Railways shall then make a general statement on railway account and working. The expenditure proposed in the railway budget, including the expenditure from the depreciation fund, and railway reserve, shall be placed before the Legislative Assembly in the shape of the demands for grants. The form the budget shall take after separation, the detail that it shall give, and the number of the demands for grants into which the total vote shall be divided shall be considered by the Railway Board in consultation with the proposed Standing Finance Committee for Railways with a view to introduction of improvement in time for the next budget if possible.

(8) These arrangements shall be subject to periodic revision but shall be provisionally tried for at least three years.

(9) In view of the fact that the Assembly adheres to the resolution passed in February, 1923, in favour of the State management of the Indian Railways, these arrangements shall hold good only as long as the East Indian Railway and the Great Indian Peninsula Railway and the existing State-managed Railways remain under the State management. But if in spite of the Assembly's resolution referred to the Government should enter on any negotiation for the transfer of any of the above railways to company management, such negotiations shall not be concluded until facilities have been given for the discussion of the whole matter in the Assembly. If any contract for the transfer of any of the above railways to company management is concluded against the advice of the Assembly, the Assembly shall be at liberty to terminate the arrangements in the resolution.

Apart from the above convention the Assembly further recommends:

(i) That the railway services shall be rapidly Indianized, and further that the Indians should be appointed Members of Railway Board as early as possible, and

(ii) That the purchase of stores for the State Railways shall be undertaken through the organization of Stores Purchase Department of the Government of India.

Committee have been substantially accepted. The railway budget has been separated from the general budget, and the control of the Finance Department practically withdrawn. The system of what was known as the revenue programme has been abolished. Every year the Government of India used to provide for the renewal of the wasting assets of the railways out of their annual receipts, but the amount so provided was not determined on any scientific or intelligible principle. It depended upon the condition of the general finance. Now a depreciation fund has been instituted to which every year a certain amount calculated on the basis of the normal life of each class of wasting assets will be credited and out of which money will be provided when the assets are worn out and have to be replaced. The amount carried to the fund will be independent of the amount actually spent in a particular year on the replacement of plant locomotives, etc. A great commercial concern like the railways should have a strong reserve to fall back upon. Every well conducted business carries in good years a portion of its profits to the reserve which can be drawn upon when the circumstances are less favourable, and a period of low or no profits has to be tided over. The Indian railways have so far been managed without any provision for reserve. It is now proposed to remove this defect and build up a reserve to make the railway finance more elastic and make provision for the equalization of dividends. Freedom from the control of the Finance Department will make it possible for the railway administration to introduce a system of finance more suited to a vast commercial undertaking. "The primary function of such (Finance) Department," to quote the Acworth Committee once more, "is to reduce to minimum expenditure in order to keep at the minimum the corresponding taxation. Its officials are not qualified either by training or experience to judge the essentially commercial and technical questions, where and when the circumstances of a railway undertaking justify expenditure of large sums, having regard not only to the actual conditions of the physical machine at the moment, but to the prospect of development and requirement of the future." The separation of railway finance will have another important effect. The determination of railway rates is a very intricate business. It involves consideration of a number of complex issues. The railway charges for different categories of goods cannot be fixed

according to the estimated cost of service. In calculating the schedule of rates the local conditions, the capacity of a particular industry or a particular tariff to bear particular rates, future possibilities of development, and various other factors and their interactions have to be taken into account. It is impossible to fix the rates on the basis of well-accepted principles of railway finance if these delicate arrangements are to be disturbed to suit the general budget of a particular year. In 1916 surcharges on railway traffic were imposed to meet the exigencies of general budget and were subsequently enhanced in 1921 for the same reason. This was done because there was no time to await proposals for the readjustment of railway rates to bring in additional revenue. It was pointed out by railway administration and the commercial bodies that the incidence of surcharges would be inequitable and upset the calculations of the experts regarding the ability of different kinds of traffic to bear the particular rates. But in view of the pressing need for additional revenue their protests were disregarded. The separation of railway finance will leave the railway managers free to fix the rates and fares on the principle of "charging what the traffic will bear," and make the taxation of transport, which is obviously undesirable, almost impossible. The railway administration will now be in a position to adopt a well-considered programme of development and extension with an assurance that the funds would be available for carrying it out. The system according to which the unspent balance of money alloted for railways "lapsed" at the end of the year would become a thing of the past.

The financial provisions of the new convention are, of course, very important. They are contained in clauses two and three of the Resolution. The relation of railway receipts to the general revenues is a matter with regard to which there can be a difference of opinion. The one view is that after the Railway Department has paid its working expenses and the interest charges it should be free to regulate the balance of its receipts in its own way subject, of course, to the general control of the Government and the Legislature. The view, however, has not got many adherents in the country; and the general view which is gaining ground, is that the railways should make a decent contribution to the Treasury, specially in view of the fact that in the past for a number of years taxation had to be imposed

to meet that portion of interest which the railway receipts could not cover. It has, however, to be borne in mind that any figure that might be taken for the contribution must be more or less of an arbitrary character. The present arrangement provides for a contribution of 1 per cent on capital at charge on all commercial lines at the end of penultimate financial year, plus one-fifth of the surplus profits remaining after the payment of the fixed contribution. The contribution of 1 per cent has to be paid year by year, and is to be the first charge on the net receipts of the railways. Railways take the risk of the season. Their receipts depend upon the condition of the trade and monsoon-factors, which are liable to great variations. Capital sunk in new lines does not, as is well known, yield return till years after its investment. But the contribution of railways to the general revenues begins from the year of its investment. Besides the contribution of 1 per cent and a share of profits, the general revenues are entitled to receive one-third of any excess over three crores of surplus remaining after the above payment has been made, which amount is to be transferred to the reserve.[1] The uses to which the reserve is to be applied have also been specified in the Resolution. It is to be used to meet the fixed contribution to the general revenues if the receipts in a particular year are inadequate for the purpose. The arrears of depreciation can be made up by drawing upon the reserve, and if the amount therein is large enough to warrant the adoption of such a course, it can be dissipated in the form either of the improvement of services or reduction of rates. These arrangements are provisional, and will be revised, if necessary, after three years.

When the proposal for the separation of railway finance was under consideration, there were entertained some misgivings

[1] The working of this provision can be illustrated by the contribution of railways to the general revenues for the year 1924–25:

In that year, according to the revised estimates, profits from commercial lines amounted to Rs.11,24,58,000. The contribution of 1 per cent on capital at charge came to Rs.5,40,42,000, and one-fifth of the surplus profits to Rs.90,00,000. The loss on strategic lines during the year, which is to be borne by the general revenues, is estimated at Rs.1,50,58,000. The net contribution to the general revenues amounts to Rs.5,09,52,000. If we deduct this amount and the loss on strategic lines from the total profits, we get a surplus of Rs.4,64,48,000, out of which three crores and two-thirds of the balance of Rs.1,64,48,000 are to be placed to the reserve and the other one-third, i.e. Rs.54,83,000, accrue to the general revenues. This calculation is, for special reasons, based on the results of 1923–24.

regarding its effect on the control of the Legislature over railway receipts and expenditure. The Commerce Member took special pains to make it quite clear that the reform will not impair the efficacy of legislative control in the slightest degree. It would, if anything, make it more effective by giving the members of the Assembly better opportunities for discussing and criticizing the railway budget. The railway budget is now introduced about a week before the general budget by the Member in charge of Railways, and special days are allotted for its discussion. The budget has been split up into fifteen votes. Two of them relate to the strategic lines, and the other thirteen to commercial lines. In addition to the general budget memorandum, separate notes on each demand are circulated, and also separate statements on each and every railway that comes into the railway budget. These statements give for each railway the revised estimates for the current year, the budget estimates for the ensuing year, and to each statement an explanatory memorandum is attached. It gives an account of the working of the railways in the current year of the prospects of the next year, and of the programme of development and betterment. The Standing Finance Committee, which is to consist of twelve members, one nominated official chairman and eleven non-official members elected by the Assembly, will have the opportunity of examining the budget estimates in advance. The experience will, of course, show the directions in which the present procedure will have to be modified in order to increase the efficacy of the legislative control; but it must be admitted that the changes that have recently been introduced have undoubtedly improved matters in this respect. In the first four years of the Reforms railway expenditure received very scanty attention. There were only two railway votes and often they were summarily disposed of for want of time, most of the time available for the demands for grants being spent on comparatively trivial matters.

The importance of railways in the national economy cannot be overestimated. They are a very valuable national asset, which ought to be developed in the interest of our economic life and other reasons of wider importance. It may be hoped the new arrangements will infuse a new spirit into the management of the railways, and lead to the adoption of sound financial methods.

APPENDIX X

ALLOCATION OF REVENUES BETWEEN THE CENTRAL AND THE PROVINCIAL GOVERNMENTS

The problem of fiscal relations of the different public authorities has come to the front everywhere. This is due to two reasons. The growing public expenditure on account of the increasing complexity of social life, and the extension of public activities makes the search for new sources of revenues an imperative necessity. The public authorities of all grades are hard pressed for money, and are naturally anxious to have wider taxing powers. The other reason for this development is the breakdown of the administration of many important and time-honoured fiscal expedients on account of the growing integration of economic life. The problem has assumed an acute form in India for reasons which it is not necessary to discuss at length. The constitutional changes called for radical changes in the fiscal inter-relations of Central and the Provincial Governments in order to realize the ideal of giving to the provinces "largest measure of independence of the Government of India." But unfortunately the authors of the new constitution had to reckon with the accumulated inequalities of the past which could not be redressed at once. They knew from experience that the tangle which they had to unravel was the result of an absence of a clear line of demarcation between the duties and the resources of the Central and the Provincial Authorities; and it appeared natural to them that since the knot could not be untied, it should be cut and the resources of the Government of India completely differentiated from those of the Provincial Governments. The formula which embodied the new wisdom was that for administrative clean-cut, financial clean-cut was necessary. Each authority was to have distinct sources of revenue, and no arrangement which had the remotest "taint of the divided heads" could be allowed to continue under the new regime. The realization of the project threw certain anomalies into bold relief which till then had been hidden from

the eye by the intricate arrangements of the old order. It was unfortunate that what was implicit should thereby become explicit, and thus be exposed to the public eye ; but it was contended that it was better to face the facts of the situation squarely, recognize that they were disagreeable, and work for the future with a firm conviction that the inequalities would be smoothed out in due course, and the specific of the " clean cut " prevent the recurrence of similar complications. It was assumed that for the success of the constitutional experiment it was necessary that the Provincial Governments should have a working surplus, and thereby be made capable of introducing measures of social and economic reform. The later developments belied these expectations. Several important assumptions on which the new arrangements were based proved to be wide of the mark. The Provincial Governments, instead of having abundant resources for financing the schemes of social betterment, could not even balance their ordinary budgets. The Central Government found that equilibrium between revenue and expenditure, for the attainment of which it had incurred so much odium, could not be realized. The provinces clamoured for relief from the contributions. The Central Government had nothing better to offer in return than a renewed assurance that their reduction would be the first charge on the betterment of central revenues. The situation improved last year, and the prospect of a partial relief to the three provinces was held out by the Finance Member, but the circumstances, which are a matter of common knowledge, made it impossible for him to carry out his intentions. It is not easy to give a correct description of the present situation. It would not be wrong, though not quite apt, to call it a state of suspended animation. It is necessary to analyse briefly the fundamental features of the present arrangements, and see why and in what directions they ought to be revised, if they are to work well in the future.

The basic principles of the existing arrangements are well known. They have been clearly set forth in Chapter VIII of the Joint Report. They, unlike the settlements which they have succeeded, are not based on the estimated needs of the provinces, but aim at making them independent of the help and control of the Government of India. The complete separation of resources was considered necessary to enable them to work out their own destiny. Income-tax and tariffs were to be

assigned to the Central Government. As regards the latter head of revenue there was and can be no difference of opinion. It ought to be controlled by the Central Authority, otherwise the economic unity of the country, without which the political unity cannot be preserved, would be put in jeopardy. The arguments for making income-tax a central head were put forward with great earnestness. The most important of them were the need of uniformity of rates and that of avoiding the difficulty of assessment and administration arising out of the incomes being derived in one province and received in another. Land Revenue was to be assigned to the Provincial Governments on account of its intimate connection with the whole administration in rural areas. Excise, Judicial Stamps, Registration, Irrigation, and Forests were also to be made provincial receipts, while Salt, Opium, and Commercial Stamps were to go to the Central Government. The all-India deficit, which would result from the adoption of this scheme was to be covered by requiring each province to contribute 87 per cent of the gross surplus to the Central Exchequer. The Government of India in their despatch of the 5th March, 1919, while accepting the principle of covering Indian deficit by fixed charges on the provincial revenues, and assessing it as an all-round ratio of the gross surplus, contended that an arrangement which disclosed the true position of the provinces in the past would not, on that account, justify the continuance of the inequalities in the future. They, therefore, suggested that the initial scale of contributions, should be treated as provisional, and steps be taken to fix a standard scale on some equitable basis. The Meston Committee, which was appointed to fix a standard scale of contributions, pointed out that though the initial contributions could not be made equitable on any acceptable basis, they should in a period of seven years be changed so as to correspond in some measure to the capacity to pay of each province. It recommended that the commercial stamps should also be made a provincial head, and uniformity of rates secured by making it subject to the Indian legislation. This change was considered necessary in order to leave to each province a reasonable working surplus. The basis of the initial contributions was altered. Instead of gross surplus the basis of apportionment of the deficit was to be the additional spending power, which would be placed at the disposal of the provinces under the new arrangements. But

the contributions were not to be levied at a flat rate on account of the disparity in the financial strength of the different provinces. The major provinces of Madras, United Provinces, Punjab, Bombay, and Bengal were to surrender 60 per cent of their additional resources, Central Provinces and Assam 40 per cent on account of their small margin of surplus and the need for development, and Burma only 6½ per cent in view of its backward condition. Bihar and Orissa was recommended for complete exemption, as it was the poorest province, and the imminent liabilities which it had to meet to provide the requirements of a self-contained province would strain her resources to the utmost. The Joint Committee accepted these recommendations, but laid down that on no account should the initial contributions be raised, and standard proportion should be reached by affording relief to those provinces, which were being called upon to pay more than their due share, as soon as the condition of the central finances made the reduction of the total contribution possible. These arrangements are an integral part of the present constitution, and cannot be changed till the whole question of the revision of the latter becomes a practical issue of immediate importance.

The revision of the Meston Settlement has been urged by various parties. As things are, only the provincial contributions are receiving public attention, and their early extinction is being demanded. But the problem is more difficult, and cannot be solved merely by the cessation of contributions. The whole scheme is the result of certain presumptions, the validity of which can be questioned from a scientific standpoint. It is necessary to examine the position a little carefully. There are three important reasons why the scheme is defective and cannot give us an enduring basis for the solution of the problem. The first is that while admitting the existence of the inequalities, it makes no provision for their removal. Since 1870, when Lord Mayo introduced the first measure of decentralization, again and again the mistake of taking the existing scale of expenditure as normal has been committed. As Gokhale pointed out in his evidence before the Welby Commission, the settlement of 1870 crystallized the inequalities which had grown up on account of the distribution of resources having been effected in an arbitrary manner by the Government of India by making fixed assignments to the provinces for meeting their

respective scales of expenditure. The quinquennial settlements introduced in 1882 accentuated the differences still further. The practice of resuming the unexpended balances, and revising the settlements on the basis of the provincial expenditure at the end of the period put a premium on extravagance, and made it necessary for each province to raise the apparent scale of expenditure. The provinces which were most successful in displaying their needs received differential treatment. After the quasi-permanent settlement of 1904, which again left the inequalities unredressed, the distribution of " doles " for specific purposes had the effect of making the favourable treatment of some provinces more pronounced in certain cases. During the war some provinces adhered to economy very strictly, while others increased their expenditure more freely. The result of these successive phases of the financial history of India has been the same. There is a wide divergence between the scales of expenditure set up in different provinces. The existence of these differences is admitted, but their extent is not generally known. In Statement I the disparity is set forth in a tabular form. It was, to use the words of the Joint Report, masked by a system of divided heads in 1920. In Statement II the corresponding figures for the year 1922–23 (the year for which the actual figures of revenue and expenditure are available) are given. The comparison of the two Statements will show that the Reforms have not made any appreciable difference in this respect. It is not necessary to add that this disparity is not in the best interest of the country. If these inequalities were the result of a lack of enterprise or resources on the part of provinces concerned, it could perhaps be urged that it is the duty of the provinces, which have a long lee-way to make up, to help themselves. But when we know that it is the Government of India which is responsible for different provinces being in different stages of development, the removal of inequalities appears in a different light, and ought to be considered a charge on national revenues. It is no use relying on things righting themselves in due course. The progress of the nation as a whole is being retarded as the different provinces cannot keep pace with one another. It is very desirable that the backward provinces should have the resources for equipping themselves with the requisites, which will enable them to come in line with the more advanced neighbours. The absence of a provision for this purpose is a

very strong reason for revising the present settlement. The other reason why it should be reconsidered, is the comparative inelasticity of the provincial revenues. The figures tabulated in Statement III will show that while the sources of revenue assigned to the Government of India have, since 1911–12, moved upwards with a marked ease, the provincial heads of revenues have shown very little capacity for expansion. The Accountant-General, United Provinces, in his Appropriation Report for 1921–22 draws pointed attention to the fact that revenues derived from the provincial heads of receipts have practically remained stationary for the last five years, and emphasizes the necessity of tapping some new sources, if the progress of the provinces is not to come to a standstill. The same remark can be made with reference to all the provinces taken together. There are differences of degree. Some of the provinces have undeveloped economic possibilities, which can to a certain extent be counted upon for bringing some grist to the provincial mills after some time, but in the immediate future there is no hope in that direction. On the other hand their realization is likely to involve initial outlay, which will necessitate their being put on the wrong side of the provincial balance sheets. The situation is exceedingly unsatisfactory, and it is no wonder that it has filled the popular representatives with dismay. Though the three provinces of Madras, United Provinces, and Punjab can, if the contribution are extinguished, look forward to improving their finances considerably, all the provinces cannot feel buoyant collectively even if this pledge is fulfilled in the near future. To these reasons for the re-allocation of the resources must be added another. In most of the provinces the rural block is very strong in the legislatures, and what is more is occupying a "key" position in the party-game. It knows its power and is anxious to assert it. It is prepared to range itself against the progressive forces of the country if it can get a price for its support; and the price, as is well-known, is the revision of land revenue policy for the benefit of the landed interests. Even if the permanent settlement cannot be secured, it wants concessions which will take away whatever elasticity land revenue may possess under the present circumstances. The recommendations of the Land Revenues Committees of Madras, Punjab, and United Provinces are conclusive for substantiating the truth of this remark; and

though till now the Provincial Governments have been able to fall back upon the support of the Government of India, and ward off the attacks of the rural parties, they cannot resist the pressure for long. The land revenue policy is likely to be revised early in order to afford relief to the landed interests of the country. The result of this development, which may be taken as imminent, will be the reduction of the receipts from land revenue. Increasing pressure for a more drastic regulation of liquor traffic will also affect the provincial finances adversely, and make Excise a very precarious source of revenue. If the receipts from land revenue and excise fall off on account of these parallel movements, the provinces will find it very difficult to balance their budgets. Bombay and Bengal are the two provinces which have demanded the revision of the Meston Settlement. The other provinces want the speedy cessation of the contributions. But if a more prospective view of the situation is taken, it is in the interest of all the provinces that the question of redistribution of resources should be opened up again, and the fiscal relations of Central and the Provincial Governments established on a sound basis.

There are certain leading principles of wide application, which have to be kept in view in making these readjustments. Seligman has called them the principles of efficiency, suitability, and adequacy. The first in order of importance is the principle of efficiency. A scheme of allocation, which assigns a source of revenue to an authority which, from the nature of things, is not in a position to administer it efficiently, is doomed to failure. The effectiveness of taxes depends upon the nature of the taxes and the character of administration. A tax cannot work well in practice when the authority entrusted with its administration cannot handle the practical problems of the tax, or has not developed the traditions of efficiency and purity on which a great deal must necessarily depend. The principle of suitability is closely connected with that of efficiency. This is, as Seligman has pointed out, a problem as to the base of the taxation. The wider the basis of the tax, stronger the argument in favour of placing it in the hands of an authority with broader jurisdiction. The principle of adequacy must, it is obvious, be of very great importance, but the fact which gives it a special significance in this connection is that in certain cases it is not possible to harmonize its operation with that of the principle

of efficiency and suitability. It may be that the application of the latter will result in an adequate yield of revenue in one case or more than adequate in another. When this situation arises it becomes necessary to adopt a scheme which provides for a division of the yield of certain taxes. The principle of adequacy also implies that the revenues of each authority should be capable of natural expansion to provide for the growing needs of the body politic. When a scheme is put into operation in a country for the first time, the provision of some transitional measures, to adjust the finances of the different authorities in the State to the new conditions, may be necessary to make it possible for the new arrangements to work without friction.

In every scheme of reallocation, which can be adopted, five methods or their different combinations can be utilized. The taxes may be assessed by the Local authorities with additions for the use of the Central Government. The most familiar instance of this method is the American Property Tax. The rate of the levy is determined by the Local Authorities and to this are added rates imposed by the superior jurisdictions. The reverse of this system is the assessment by the Central Authorities with additions for local purposes. This method is known to us in the form of local cess collected for the rural boards by the Provincial Authorities. We have a more widely known illustration of this method in the four direct taxes of France, which have now been replaced by the new income-tax. The third method is the separation of resources. The separation may mean assignment of absolutely distinct sources to the different jurisdictions—the sense in which it is understood in India, and for which the Americans use a more expressive word, segregation. It may also mean that though certain sources of revenue are reserved for Central and others for the Local Authorities, there are still some common sources of revenue on which both depend. The complete separation of resources has, besides India, been adopted in some other countries, but the segregation of sources, to use the words of Sir Josiah Stamp, "is not quite the fetish that it at one time seemed to be." When separation is partial, we get the fourth method, which has already been mentioned above, the division or apportionment of the yield of the sources of revenue. According to this method the sources of revenue are completely segregated, i.e. their assessment and administration are assigned either to one author-

ity or the other, but their proceeds are divided between two or more jurisdictions in certain proportions. In the reconstruction of the German tax system this method has been utilized for fiscal arrangements. The Federal authorities control income, inheritance, land transfer, and turnover taxes, but two-thirds of income-tax, one-fifth of the inheritance tax, half of the land transfer tax, and three-twentieth of turnover tax are paid to the States for their requirements. This method is also known in other countries, and its use is becoming common on account of the difficulty of providing sufficient revenues for the different grades of governments in any other way. The last method that can be utilized is the system of payments from Central to Local Governments and from Local to the Central Government. In India the method has been adopted as a temporary makeshift, but it is possible to use it as a permanent part of our fiscal arrangements. In Canada and Australia the Federal Governments pay to the States a certain sum *per capita* in return for the surrender of the right to impose custom and excise duties by the latter. In the old German Empire, the States paid what were called the *matricular* contributions to the Central Authorities. There is nothing inherently wrong about this system, and when the relations between the different constituents of a State have been duly adjusted, its use need not offer any insuperable difficulties. The provincial contributions in India have caused very great resentment on account of certain provinces having to pay much more than others whose capacity to pay is not less, and the widespread belief that necessity for contributions arises because the Government of India incurs very heavy expenditure for defence. It is under these circumstances advisable to do away with contributions as soon as possible. But apart from this consideration it is not unthinkable that the provinces should make payments to the Central Government as a permanent measure of fiscal adjustment between the two authorities.

For us the choice lies between these methods or their combinations. It its no possible to discuss the relative merits or demerits of these methods in this paper. But the lines on which the readjustments ought, in the opinion of the writer, to be made, can be briefly indicated. The first, third, and the fifth methods do not deserve any serious consideration. The local assessment and administration of most of the taxes is impossible

under the modern conditions. The payment of contributions, though theoretically legitimate, is likely to give rise to complications which can and ought to be avoided. A complete separation will lead to fiscal embarrassments, and is on that account undesirable. The fourth method of the apportionment of the proceeds of taxes can be adopted. But it will in the beginning be difficult to fix the proportions in which the yield of taxes ought to be shared. It is not possible to go into details, but it may be stated that of the four bases of population, area, revenue, and expenditure, which can be taken into account for fixing the proportions, none will give satisfactory results in the beginning. It is a very convenient method and its use may become necessary later on, but it should not be utilized in the immediate future. The one method that is left to us, if all others cannot be used, is the centralized administration of certain taxes with additions to their rates for provincial purposes. The provinces will have certain sources of revenue which will be administered by them, and the yield of which will also go to the provincial treasury. But besides these they will have some sources of revenue in common with the Central Government, which will be administered by the latter. The two taxes which, on account of their broad base, should be administered by the Central Government, but from which the provinces can also be allowed to get revenues by way of surcharges on their rates, are income-tax and inheritance taxes. Income-tax is already an important constituent of our tax system. Inheritance tax has not even been tried as yet, but it will have to be imposed before long. It is now one of the scheduled taxes which the provinces can levy without obtaining the previous permission of the Government of India. But the provincial administration of inheritance tax will lead to very great difficulties and should not be even tried. The principle of efficiency requires that it should be administered by the Central Government. If this is conceded, then only practical solution of the problem is that the Central Government should be in charge of the assessment and administration of these taxes, and the Provincial Governments should be authorized to increase their rates within their jurisdiction. The arrangement will work well provided three difficulties which will arise in this connection can be overcome. If the Provincial Governments impose high rates for their purposes, it may happen that the

combined central and provincial taxes will become so heavy that they, besides causing injustice to the persons concerned, will affect the productivity of the taxes themselves. This possibility, however, can be obviated if the maximum limits up to which the rates can be enhanced by the Provincial Governments are prescribed by the Government of India. The other difficulty which can be easily anticipated, and will have to be provided for, is the difficulty of double taxation due to the source and the recipient of income not being coterminous. The same difficulty will arise on account of the location of property, and the residence of its owner being different. This difficulty can be got over by laying down some rules as to the relative proportion to be taken by each taxing authority. Here again the supervision of the Government of India will be required in order to bring about uniformity in all the provinces; and if all the provinces adopt the same plan, the smooth working of the arrangement can be ensured. The third difficulty to be considered in this connection is not serious and can be easily solved. As the taxes will be assessed and collected by the same agency, the cost of their administration will have either to be shared between the Provincial Governments and the Central Government, or it will have to be completely met by the latter. The increase in the cost of maintenance of a central agency for the administration of these taxes on account of its having to collect the provincial surcharges as well, will not be very heavy, and can easily be defrayed out of the central revenues. As for the assessment of income and property concerned, all that need be done is that the assessees should duplicate for provincial purposes the returns submitted by them to the assessing officers. The collection of the additional taxes for the provinces will entail extra expense, but it will not be heavy and can be placed either on the provincial or the central estimates by mutual agreement. This arrangement will not in any way militate against the autonomy of the provinces. The provinces should have, within the spheres assigned to them, complete liberty to manage their finances in their own way without any outside interference. The administration of taxes will, however, be under the control of the Government of India, and the provinces will determine their own rates. The scheme will give elasticity to the provincial revenues. The efficiency of administration will not suffer.

The rates will not be allowed to become unduly heavy, and there will be no conflict between the different taxing authorities. This method can only be applied to the direct taxes. The custom and excise duties should be the same throughout the country, and their administration centralized. The yield of taxes on liquors and intoxicating drugs should go to the provinces as at present, but the difference in rates and diversity in methods of administration should not be allowed to continue. These reforms, if carried out, will mean a considerable improvement on the existing state of things ; and if they have been given a fair trial for sometime, and still the provinces or the Government of India need more money, the method of the division of yield may be used. But it will not be necessary to have recourse to it for some time to come.

These proposals practically mean revival of the divided heads in another form, which we have been taught to believe are wrong in principle, and create unnecessary intricacies. The scheme of the absolute separation of resources is simpler, and should certainly be preferred if it can give us a satisfactory distribution of resources. But if that is not possible, the alternative is to work out a scheme, which, if less simple, will be more in accord with the facts of economic life. It is not the divided heads of receipts which were responsible for the circumspection of the financial powers of the provinces. That was due to the fact that the Provincial Governments had to submit their budgets to the Central Finance Departments for approval, and the latter made meticulous alterations in the proposals of the Provincial Authorities. With the grant of final powers to the Provincial Governments over their budgets, no apprehensions need be entertained with regard to their financial powers being curtailed by their having some sources of revenue in common with the Government of India. It is a pity that these proposals have a somewhat superficial likeness with the arrangements which are associated in our minds with extreme centralization and absence of scope for initiative on the part of Provincial Authorities. But the fact in itself should not prevent us from making changes, which are essential for a more scientific allocation of resources between the Central and the Provincial Governments.

In conclusion a few words may be said about the need for levelling up the scale of expenditure in the provinces in which

it is unduly low. The provinces which have a low scale of expenditure are entitled to special help from the central revenues. They owe their unsatisfactory position to their having received less than their due in the past. They should for a number of years receive special grants from the central revenues to enable them to work up to the level of the other provinces. For this provision cannot be made in any scheme, which is intended to serve as an enduring basis of financial settlement. The only way in which this can be done is to guarantee to these provinces annual payments for a number of years to make it possible for them to adopt a programme of continuous development. These grants should neither be treated as "doles" nor as "subventions." They will be a means of making belated amends to the provinces, which have suffered from unmerited neglect in the past. The amounts of the grants to be given in this way should be determined by the needs of the provinces that have to receive them. No other measure is possible. The cases of Bihar and Orissa, Central Provinces, and Assam deserve special consideration in this respect.

ANNEXURE TO APPENDIX X

Statement I, showing the financial position of the Provinces in 1920–21.

1	2	3	4	5	6	7
Provinces.	Revenue collected per capita.	Revenue contributed to C.G. per capita.	Percentage of col. 1 to col. 2.	Provincial Revenue per capita.	Expenditure per capita.	Expenditure on General Admn. per 100.
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Madras .	5·3	2·9	55%	2·4	2·7	7·6
Bombay .	19·3	13·6	69%	5·85	6·53	25·6
Bengal .	7·35	5·5	70·45%	1·85	1·97	8·15
United Provs.	3·25	1·29	40%	1·96	2·22	7·6
Punjab .	5·9	2·55	43%	3·35	3·7	13·4
Burma .	17·8	5·7	31%	12	6·7	23·1
Bihar & Orissa	1·48	·38	25·6%	1·1	1·32	5·6
Central Provs.	3·2	·76	23·7%	2·48	3·1	10·35
Assam . .	3·7	·49	16·3%	2·5	2·65	13·6

	8	9	10	11	12	13
Provinces.	Expenditure on G.A. per square mile.	Expenditure on Education per 100.	Expenditure on Law and Justice per 100.	Expenditure on Police per 100.	Expenditure on Police per sq. mile.	Expenditure on Public Health per 100.
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Madras .	20·17	32	35	41·6	132	16·7
Bombay .	39·8	74·5	57	90	143	30
Bengal .	50·5	23·4	36·1	35·2	218	10·8
United Provs.	31·9	26·5	28·8	37·1	166	8·55
Punjab .	27	36·1	44	47·8	96	15·8
Burma .	12·9	35·5	58·1	140	78·5	26·3
Bihar & Orissa	27·6	15·9	23·4	20·4	83·5	5·6
Central Provs.	15	30·65	40·13	40·26	56	11·4
Assam . .	18·6	25	23	39·36	55·6	14·3

Statement II, showing the financial position of the Provinces in 1922–23.

1	2	3	4	5	6	7
Provinces.	Revenue collected per capita.	Revenue contributed to C.G. per capita.	Percentage of col. 1 to col. 2.	Provincial Revenue per capita.	Expenditure per capita.	Expenditure on General Admn. per 100.
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Madras .	5·35	2·35	44%	2·95	2·96	30
Bombay .	21·2	14	66%	7·3	7	58·8
Bengal .	7·2	5·05	70%	2·1	2	25
United Provs.	3·02	·78	26%	2·25	2·35	30
Punjab .	5·3	1·26	24%	4	4·3	47
Burma .	12·9	5·65	44%	6·6	7·75	67
Bihar & Orissa	1·65	·2	12·2%	1·45	1·36	20·3
Central Provs.	4·1	7·2	17·5%	3·7	3·5	34
Assam .	2·9	·48	16·5%	2·42	2·65	33·5

	8	9	10	11	12	13
Provinces.	Expenditure on G.A. per square mile.	Expenditure on Education per 100.	Expenditure on Law and Justice per 100.	Expenditure on Police per 100.	Expenditure on Police per sq. mile.	Expenditure on Public Health per 100.
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Madras .	90	36	22·3	48	143	15·2
Bombay .	92	88·5	33·5	89	139	31·5
Bengal .	151	26·8	24·1	39·5	240	16·6
United Provs.	125	30·6	14·5	38	156	8·65
Punjab .	96·5	47·5	21	58	120	19
Burma .	38	50	36	105	60	28·5
Bihar & Orissa	83	15·7	9·9	23·4	96	5·9
Central Provs.	47·7	37·8	22·1	40·5	56·3	12·7
Assam . .	47·5	30	11·8	40	57·5	16·7

Statement III, showing the receipts from the Major Central and Provincial heads of revenues from 1911–12 to 1922–23.

Heads of Revenues.	1911–12.	1912–13.	1913–14.	1914–15.
Central.	Rs.	Rs.	Rs.	Rs.
Customs .	9,70,28,499	10,79,58,640	11,33,73,302	9,52,08,010
Income-tax .	2,47,93,181	2,61,35,963	2,92,53,745	3,05,50,999
Salt . .	5,08,68,180	5,00,15,605	5,16,79,577	5,86,61,841
Opium . .	8,94,19,170	7,68,68,873,	2,43,73,178	2,35,83,274
Provincial.				
Land Revenue	31,14,70,456	31,92,37,015	32,08,73,629	31,83,23,088
Excise . .	11,41,46,285	12,41,68,787	13,34,14,505	13,28,53,214
Stamps . .	7,22,26,940	7,60,36,726	7,97,74,387	7,62,30,650
Forest . .	2,92,82,689	3,22,95,131	3,34,48,081	2,97,09,784
Registration .	66,87,937	72,30 337	77,84,426	72,79,423

Heads of Revenues.	1915–16.	1916–17.	1917–18.	1918–19.
Central.	Rs.	Rs.	Rs.	Rs.
Customs .	8,81,08,293	12,98,87,728	16,55,48,819	18,18,09,614
Income-tax .	3,13,51,643	5,65,94,498	9,46,21,555	11,63,76,940
Salt . .	5,47,13,802	7,23,93,891	8,24,92,306	6,41,69,830
Opium . .	2,87,02,712	4,74,00,073	4,61,83,538	4,93,36,670
Provincial.				
Land Revenue	33,04,67,411	33,06,18,976	32,41,08,686	31,63,49,164
Excise . .	12,94,83,132	13,82,38,495	15,24,25,600	17,33,62,773
Stamps . .	8,15,04,487	8,66,50,437	8,59,12,830	9,02,84,633
Forest . .	3,11,16,367	3,70,61,930	4,09,69,258	4,68,18,832
Registration .	77,83,187	81,08,728	79,13,852	85,89,774

Heads of Revenues.	1919–20.	1920–21.	1921–22.	1922–23.
Central.	Rs.	Rs.	Rs.	Rs.
Customs .	22,48,32,802	31,89,85,157	34,40,98,381	41,34,65,362
Income-tax .	23,20,78,443	22,19,28,478	22,17,54,823	18,13,94,485
Salt . .	5,74,79,319	6,76,45,308	6,34,37,848	6,82,46,112
Opium . .	4,55,62,212	3,53,41,234	3,07,24,798	3,78,92,068
Provincial.				
Land Revenue	33,91,49,146	31,97,48,469	34,12,17,273	35,35,16,327
Excise . .	19,25,94,029	20,43,65,359	17,18,61,914	18,55,21,656
Stamps . .	10,91,17,665	10,95,68,483	10,88,06,852	11,95,16,740
Forest . .	5,36,75,794	5,41,43,496	5,83,28,656	5,52,14,073
Registration .	1,07,54,940	1,12,03,534	1,13,55,677	1,20,44,870

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G.I. = Government of India Act 1919. R. = Rule
S. = Section. D.R. = Devolution Rules.